

Mexico: Arrangement Under the Flexible Credit Line and Cancellation of the Current Arrangement—Staff Report; Staff Supplement; and Press Release on the Executive Board Discussion

In the context of the arrangement for Mexico under the Flexible Credit Line and the cancellation of the current arrangement, the following documents have been released and are included in this package:

- The staff report on the arrangement for Mexico under the Flexible Credit Line and cancellation of the current arrangement, prepared by a staff team of the IMF, based on information available as of March 17, 2010. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A staff supplement of March 17, 2010, on the assessment of the impact of the proposed flexible credit line arrangement on the Fund's finances and liquidity position.
- A Press Release summarizing the views of the Executive Board as expressed during its March 25, 2010, discussion of the staff report that completed the request.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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**International Monetary Fund
Washington, D.C.**

INTERNATIONAL MONETARY FUND

MEXICO

Arrangement Under the Flexible Credit Line and Cancellation of the Current Arrangement

Prepared by the Western Hemisphere Department
(In consultation with other Departments)

Approved by David J. Robinson and Aasim Husain

March 17, 2010

Summary

- **Background.** Mexico is emerging from the crisis with strong fundamentals. A very strong policy framework and the authorities' quick response helped cushion the blow of the global crisis. Balance sheets have absorbed the large shock and remain strong. The authorities have demonstrated their commitment to tackling medium-term challenges, including through a tax package in 2010.
- **Outlook.** The recent upward trend in output is expected to continue, leading to projected growth of 4 percent for 2010. Financial inflows are projected to gradually resume, reflecting a normalization of global liquidity conditions. However, global downside risks are a concern later this year and into 2011. Mexico remains vulnerable to possible risks from a spike in global risk aversion and the consequent reversal of cross-border flows and nonresident investor stock positions in its large and liquid asset markets.
- **FCL.** In this context, and given the expiration of the swap line with the Fed, the authorities believe that access under a successor one-year FCL arrangement in an amount equivalent to SDR 31.528 billion (1,000 percent of quota), to replace the one-year arrangement approved on April 16, 2009—which they would like to cancel—would support their macroeconomic strategy. The authorities intend to continue to treat the arrangement as precautionary. The staff assesses that Mexico meets the qualification criteria for access to FCL resources specified under the Board decision on FCL arrangements, and recommends approval of the arrangement.
- **Fund liquidity.** The proposed commitment of SDR 31.528 billion would have a very substantial, but manageable impact on the Fund's liquidity.
- **Process.** An informal meeting to consult the Executive board on a possible FCL arrangement for Mexico was held on March 10, 2010.
- **Team.** This report was prepared by a staff team led by Vikram Haksar, comprising Ivanna Vladkova Hollar, Man-Keung Tang (all WHD), Bikas Joshi (SPR), Jose Giancarlo Gasha (MCM) and Geremia Palomba (FAD).

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I. CONTEXT

Strong fundamentals

1. ***Mexico had a very strong macroeconomic performance for over a decade coming into the crisis.*** Inflation was kept at low levels and expectations have remained well anchored. Public debt levels were reduced, including for public external debt. The external current account deficit was contained, while reserves were built to levels that were considered comfortable. Corporate sector balance sheets had likewise been strengthened, with low leverage and high profitability. Meanwhile, the banking system was highly profitable and well-capitalized, with low foreign borrowing and little exposure to structured financial products.
2. ***Underpinning this success has been a high level of policy credibility.*** Banxico's inflation targeting regime has worked well and the central bank has developed strong anti-inflation credentials. This has allowed the flexible exchange rate to work as a key shock absorber. Fiscal policy has been guided by the balanced budget rule, as well as the demonstrated commitment of the authorities to take measures to bolster the structural fiscal position, including major tax reforms in 2008 and 2010. Meanwhile, the 2006 FSAP update acknowledged the strength and sophistication of the financial sector supervisory framework.
3. ***These broad strengths have been recognized by the Board in the 2010 Article IV consultation, concluded on March 10, 2010*** (see IMF Country Report No. 10/71). Directors commended the authorities for their sound policy frameworks and progress in strengthening public and private sector balance sheets, which had enabled an effective counter-cyclical policy response and helped preserve stability during the crisis. Their swift action to secure contingent credit lines—from the U.S. Federal Reserve and the Fund—also helped maintain external confidence. Directors welcomed the progress in fiscal reforms over the past three years and the agenda to seek expenditure savings and further strengthen tax administration. They agreed that monetary policy and communication had been appropriate, with the flexible exchange rate playing an important role in the adjustment process. Directors also noted the resilience of the financial system, underpinned by strong regulation and supervision.

Crisis impact and policy response

4. ***The crisis generated a sharp output contraction in Mexico during the first half of 2009 reflecting a confluence of severe shocks.*** Close trade and financial linkages exposed Mexico to strong spillovers from the plunge in manufacturing production and asset prices in the U.S. The unanticipated large losses on corporate foreign currency derivative exposures added to market concerns about Mexican firms, further undermining their access to financing. In addition, Mexico experienced a serious outbreak of the H1N1 virus in April–June 2009, which is estimated to have reduced annual GDP by ½ percentage point. Thus, despite having entered the crisis with very strong fundamentals, Mexico's real GDP fell around 6½ percent in 2009—the sharpest contraction among Latin American peers.

5. ***Nonetheless, stability has been maintained, in part reflecting forceful and broad-based policy responses.*** For the first time in many years, a substantial countercyclical macro policy response was possible. A fiscal impulse of about 2½ percent of GDP was delivered in 2009 and policy rates reduced by a cumulative 375 bps since mid-2008. The authorities took prompt and effective steps to maintain orderly conditions in a variety of market segments, providing liquidity as needed and taking more direct steps where required. This has yielded a broad stabilization of domestic financial markets. Banxico has also intervened to provide liquidity to the foreign exchange market while preserving the most essential elements of the flexible exchange rate regime. Stability was also supported by arranging contingent external finance through a US\$30 billion swap line with the Federal Reserve—which expired on February 1, 2010 in Mexico as well as in the other countries that reached similar agreements with the Federal Reserve—and a US\$47 billion (1,000 percent of quota) arrangement under the Flexible Credit Line (see also discussion in IMF Country Report No. 10/71).

Emerging from the crisis

6. ***Mexico has emerged from the downturn with continued strong fundamentals.*** Public debt levels have risen only moderately on the back of stimulus financed to a large degree with nondebt creating flows, and debt levels remain at the lower end of other G-20 members (with gross debt at 44½ percent of GDP and net debt at 39 percent of GDP). Inflation expectations remain well-anchored. Reserves have been rebuilt to pre-crisis levels, benefiting from strong public sector forex cash flows in late 2009. Meanwhile, banks have thus far seen only a modest rise in NPLs and maintained healthy capital ratios.

7. ***Indeed, the near-term outlook is positive.*** With manufacturing exports providing impetus, the recent upward trend in output is expected to continue, leading to projected growth of 4 percent for 2010 and 4½ percent for 2011, with short run risks to the upside, especially if additional stimulus measures are implemented in the United States. While headline inflation is expected to increase in the short term as a result of recent increases in taxes and administered prices, it is expected to come down to the 3 percent target by end-2011. Financial inflows are projected to gradually resume, reflecting a normalization of global liquidity conditions.

8. ***In addition, the authorities are taking steps to address concerns underscored by the crisis.*** To ensure medium term fiscal sustainability, a significant tax package (yielding over one percent of GDP) was approved in late 2009, even in the context of a cyclically very weak economy, to offset the impact of declining oil production. Measures to further strengthen the financial stability framework are under consideration, and steps have been taken to strengthen monitoring and control of corporate derivative positions. On the structural side, significant steps have recently been taken to improve the efficiency of the electricity sector, and reforms to strengthen competition and improve labor market flexibility are at an advanced stage of preparation. (For a further discussion of these issues, see IMF Country Report No. 10/71).

9. ***Nonetheless, investor sentiment toward Mexico has weakened relative to other emerging markets, reflecting some reappraisal of fundamentals.*** The increase in risk spreads through the crisis has been somewhat wider for Mexico than for many of its emerging markets peers, the recent improvement notwithstanding. This reflects some revised views of risks from low potential growth, declining oil production, and moderate reserve cover relative to many emerging market peers (see ¶11) as well as Mexico's relatively close linkages to the United States, the epicenter of the global crisis, where potential growth is expected to be subdued in the next years.

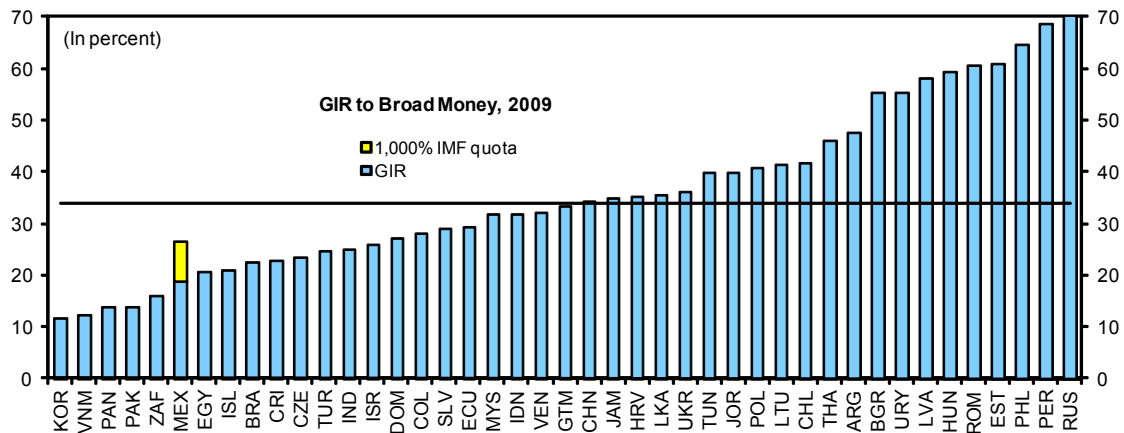
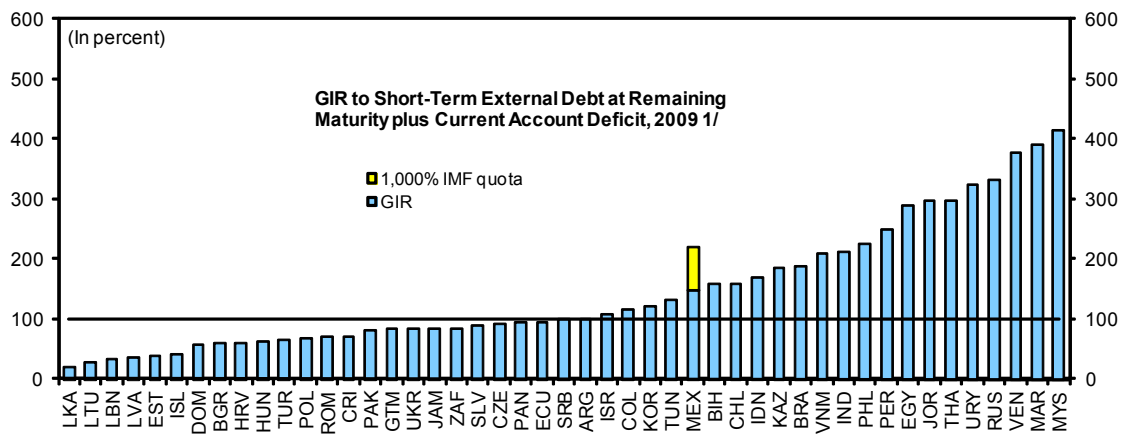
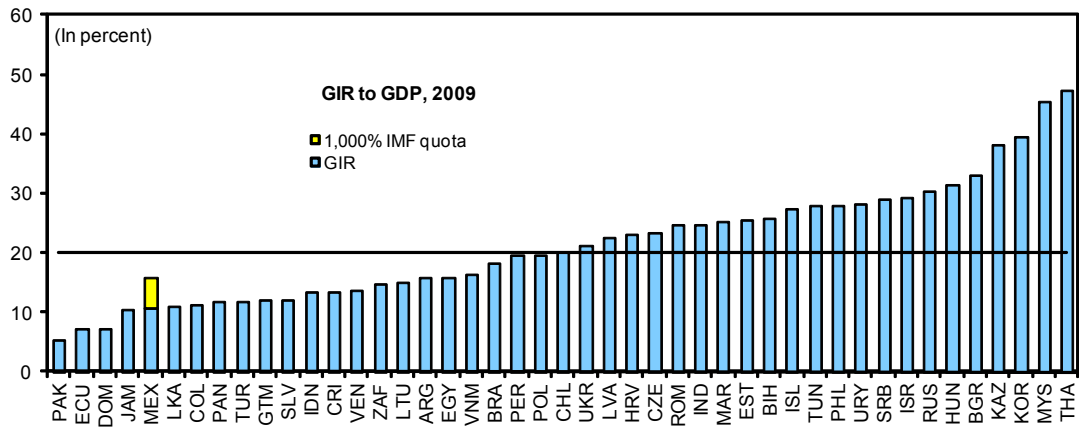
10. ***Moreover, global downside risks are a concern later this year and into 2011.*** These include the possibility that prospective large public sector debt issuance by advanced economies could intensify global funding pressures and sharply increase financing costs for emerging markets such as Mexico. Furthermore, Mexico remains vulnerable to possible risks from a spike in global risk aversion—for example from advanced country sovereign debt problems or global asset price deflation—and the consequent reversal of cross-border flows and nonresident investor stock positions in its large and liquid asset markets.

II. ROLE OF THE FLEXIBLE CREDIT LINE

11. ***Given the experience during the crisis—and the continued complex and risky global environment—the authorities believe that Mexico needs to preserve insurance against external risks.*** They view the external environment as continuing to pose substantial risks, including due to the continued volatility in international financial markets, the sharp rise in public debt in many countries, and its potential impact on growth and financing conditions worldwide. Moreover, while Mexico's reserves meet standard rules of thumb on flow variables, with coverage well in excess of maturing debt, they are low relative to peers with respect to balance sheet measures (Figure 1), which adversely affected market confidence during the crisis period.

12. ***The authorities believe that a successor FCL arrangement, which they would again intend to treat as precautionary, could play an important role in supporting Mexico's economic policy strategy in a continued difficult external environment.*** In particular, another FCL arrangement would provide insurance against still present tail risks in the period ahead. The authorities' view is that it would help them maintain an appropriate level of external insurance—considering also the end of the US\$30 billion Fed swap line. They have also noted that if, as part of the current review of the Fund's mandate, the international community were to offer emerging markets a set of suitably strong alternatives to self-insurance, this would be a factor to consider in their reserve accumulation strategy. Meanwhile, they plan to gradually build up their own reserves, which would serve to support a gradual exit strategy from the FCL.

Figure 1. Mexico: Reserve Coverage in International Perspective

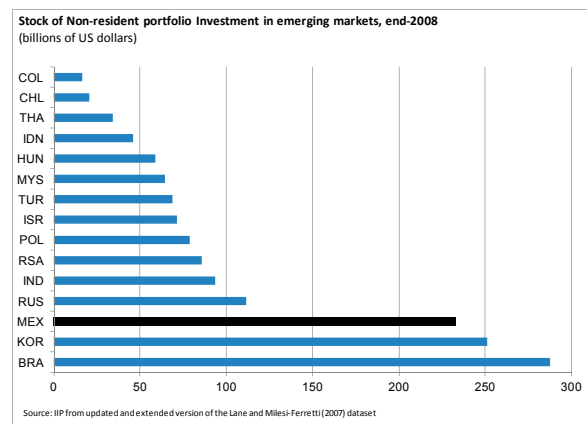


Sources: Haver Analytics; World Economic Outlook; and IMF staff estimates.

1/ GIR at the end of 2009 in percent of ST debt at remaining maturing and current account deficit in 2010. The current account is set to zero if it is in surplus.

13. *Access under a precautionary FCL for Mexico is proposed to remain at the current level of some US\$48 billion (SDR32 billion, 1,000 percent of quota) in the context of a one-year arrangement.* Factors to take into account when considering the proposed access include the following:

- **No Fed swap.** The expiration of the US\$30 billion Fed swap line has substantially reduced contingent insurance. Recourse to high access FCL resources would provide an important signal of continuity and help ensure a continued smooth adjustment to the new equilibrium without the Fed swap line;
- **Downside risks.** Continued high access is needed to provide credible assurances of sufficient liquidity under a severe stress scenario. While tail risks have diminished in the last year, the staff's preliminary analysis suggests that even a moderate stress scenario could yield a reserve drain of some US\$20 billion, reflecting downside risks to the private capital account on bond issuance, portfolio and direct investment flows (see the discussion in Box 1);
- **Non-resident exposures.** While the stress scenarios above take into account some portfolio outflows, these are hard to predict, and the scenario is moderate. Mexico continues to have very large non-resident investments in portfolio equity and domestic and external debt instruments, both in absolute terms and relative to reserves. This generates additional tail risks, especially in the face of a global systemic shock—pointing to the need for additional buffers;
- **Reserve coverage.** The authorities' goals of increasing reserves to assuage concerns about weaker coverage relative to peers versus balance sheet risks. This will happen only gradually and in this period, contingent access to FCL resources would provide needed assurance against downside tail risks.



Box 1. Adverse Scenario

An adverse illustrative scenario developed by staff suggests a possible financing shortfall of some US\$20 billion. This scenario draws on the current WEO and GFSR analysis of downside risks and assumes that the growth momentum arising from stimulus in advance countries peters out in late 2010, with large post-crisis financing needs from other sovereigns generating pressures on Mexico (as well as other EMs). The underlying assumptions in this scenario (relative to the baseline) are as follows:

Mexico. Calculations of financing shortfalls in 2010
(In billions of U.S. dollars)

| | Baseline | | | | | | Adverse scenario | | Financing Shortfalls |
|---------------------------------------|----------|-------|-------|-------|-------|----------|------------------|----------|----------------------|
| | 2006 | 2007 | 2008 | 2009 | 2010 | Rollover | 2010 | Rollover | |
| Current account | -4.4 | -8.4 | -15.9 | -5.2 | -14.0 | | -17.9 | | -3.9 |
| Net exports, oil | 19.4 | 17.5 | 15.0 | 10.4 | 4.5 | | 3.8 | | -0.7 |
| Net transfers (incl. remittances) | 25.9 | 26.4 | 25.5 | 21.5 | 21.5 | | 18.2 | | -3.3 |
| FDI | 14.0 | 19.1 | 22.0 | 3.8 | 17.5 | | 14.4 | | -3.1 |
| Public sector, MLT flows | 23.5 | 32.3 | 32.9 | 32.9 | 20.4 | 2.3 | 19.0 | 2.1 | -1.4 |
| Private sector, MLT flows | 14.9 | 19.8 | 12.6 | 20.2 | 19.0 | 1.2 | 15.6 | 1.0 | -3.4 |
| Short-term financing | 20.7 | 22.5 | 25.2 | 28.5 | 24.3 | 1.1 | 20.6 | 0.9 | -3.7 |
| Portfolio and other investment assets | -12.2 | -21.8 | -7.9 | -11.3 | -6.0 | | -10.5 | | -4.5 |
| Total identified shortfall | | | | | | | | | -20.1 |

- Current account pressures arise from lower U.S. growth and depressed oil prices. While non-oil net exports are expected to be unaffected (as import content of exports remains high), the assumed 15 percent decline in oil prices (about 20 percent probability based on latest futures distribution) over the baseline of US\$70.8 per barrel is projected to reduce net oil exports by US\$¾ billion. Further, a slowdown in the U.S.—and continued high Hispanic unemployment rate—would lower remittance receipts by some US\$4 billion.
- FDI is assumed to fall almost 20 percent relative to the baseline, yielding a gap of about US\$3¼ billion. Foreign direct investment has tended to be volatile, with net investment in 2009 declining not only due to lower FDI inflows, but also due to a few large investments abroad by Mexican firms seeking expansion opportunities.
- While high sovereign financing requirements may be a likely driver of heightened global stress, the Mexican public sector would remain largely insulated due to its limited external amortization needs in 2010. For public sector financing from capital markets, the scenario assumes 100 percent rollover of projected amortization needs and ¥150 billion of pre-financing for 2010, with no additional bond issuance. MLT financing from multilaterals is unaffected. This yields a modest financing shortfall of US\$1½ billion.
- The private sector is assumed to be more constrained in meeting its financing needs, accounting for some US\$12 billion of the total financing need:
 - On MLT flows, rollover rate is at 100 percent, with no new net financing assumed. This represents a decline of 20 percent from baseline for 2010—but around the preliminary estimate for rollover in 2009—and yields a financing shortfall of US\$3½ billion.
 - On short-term financing, rollover declines to 90 percent—the average level observed pre-crisis—creating a financing shortfall of US\$3¾ billion.
 - Portfolio and other flows experienced the most stress during the 2008–09 period, and the adverse scenario assumes a milder resumption of such pressures. Given the volatility of the series, the scenario assumes a two standard deviation shock, yielding a shortfall of almost US\$4½ billion. At the height of the recent global crisis—over 2008Q4–2009Q1—outflows in portfolio investment alone accounted for about US\$6¾ billion.

14. **The access being requested under the FCL arrangement is not out of line compared with other recent high access cases.** The table below compares the access level being requested by Mexico under the FCL to the broader experience of other high access cases in the Fund, across an array of metrics. Access for Mexico at the 1,000 percent level is at or below the median of high access cases on many measures, including as a share of GDP (5 percent), trade (<20 percent of exports or imports), and broad money (8 percent).

Mexico: Proposed Access, 2010

| | Proposed Arrangement | Mexico FCL April 17, 2009 | Poland FCL May 6, 2009 | Colombia FCL May 11, 2009 | High-Access Cases 1/ | | | |
|--|----------------------|------------------------------|---------------------------|------------------------------|--------------------------------------|----------------------------|-----------------|--------|
| | | | | | Proposed Arrangement (Percentile) | 20th Percentile (Ratio) | 80th Percentile | Median |
| | | | | | | | | |
| Access | | | | | | | | |
| In millions of SDRs | 31,528 | 31,528 | 13,690 | 6,966 | 100 | 1,169 | 12,903 | 5,276 |
| Average annual access (percent of total) | 1,000 | 1,000 | 1,000 | 900 | 100 | 165 | 525 | 244 |
| Total access in percent of: 2/ | | | | | | | | |
| Actual quota | 1,000 | 1,000 | 1,000 | 900 | 83 | 300 | 941 | 559 |
| Gross domestic product | 5 | 6 | 5 | 5 | 38 | 3 | 9 | 6 |
| Gross international reserves | 44 | 49 | 34 | 44 | 39 | 27 | 84 | 49 |
| Exports of goods and nonfactor services | 17 | 19 | 11 | 33 | 34 | 11 | 39 | 23 |
| Imports of goods and nonfactor services | 16 | 17 | 11 | 29 | 36 | 10 | 33 | 20 |
| Total debt stock | | | | | | | | |
| Public | 12 | 10 | 10 | 15 | 42 | 9 | 33 | 15 |
| External | 24 | 24 | 8 | 22 | 89 | 7 | 20 | 12 |
| Short-term external 3/ | 105 | 77 | 21 | 84 | 84 | 20 | 102 | 36 |
| M2 | 8 | 10 | 11 | 34 | 21 | 8 | 30 | 15 |

Source: Executive Board documents, MONA database, and Fund staff estimates.

1/ High access cases include available data at approval and on augmentation for all the requests to the Board since 1997 which involved the use of the exceptional circumstances clause or SRF resources and arrangements under the FCL. Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previously approved and drawn amounts.

2/ The data used to calculate ratios is the actual value for the year prior to approval for public and short-term debt, and the projection at the time of program approval for the year in which the program was approved for all other variables

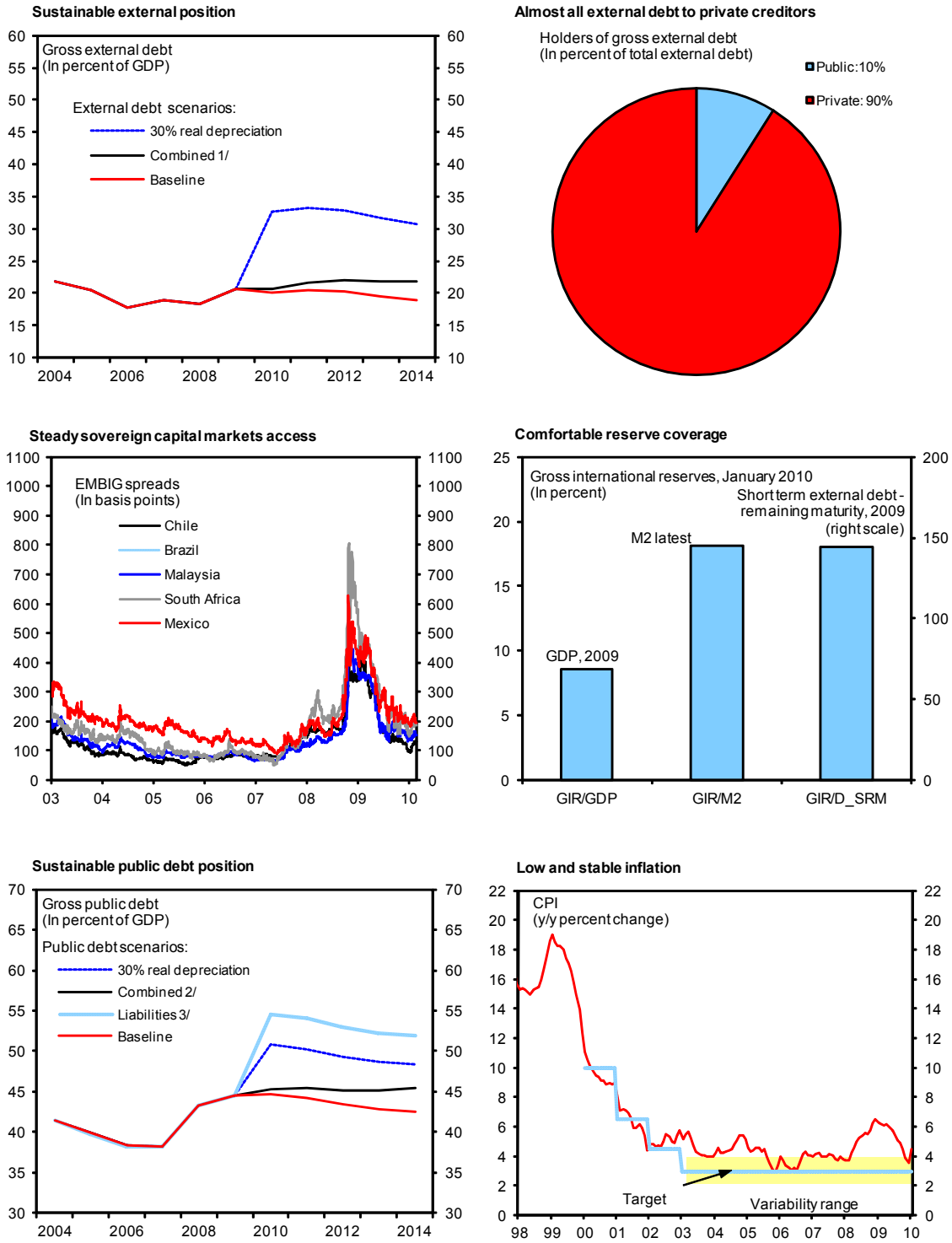
3/ Refers to residual maturity.

Qualification criteria

15. **The staff believe that Mexico qualifies for an arrangement under the FCL** (Figure 2). The authorities continue to have in place a very strong policy framework, elements of which in Mexico's case include successful inflation targeting, a credible fiscal rule, and strong bank regulation and supervision. The important tax measures approved in the 2010 budget again demonstrates the authorities' commitment to maintain very strong policies, as acknowledged by the Board during the recent 2010 Article IV consultation.

- **Sustainable external position.** External debt levels are projected to decline from current moderate levels of around 24 percent of GDP to around 20 percent of GDP over the medium term, with public external debt remaining low as well. Among other factors, this reflects the projected external current account deficit being contained at about 1½ percent of GDP. These findings are generally robust to a range of shocks as discussed in the DSA analysis in IMF Country Report No.10/71.

Figure 2. Mexico: Qualification Criteria



Sources: Bloomberg L.P.; Datastream; EMED; Haver Analytics; and IMF staff calculations.

1/ Combined permanent 1/4 standard deviation shocks applied to interest rate, growth, and primary current account balance.

2/ Combined permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

3/ One-time 10 percent of GDP increase in debt-creating flows.

- **Capital account position dominated by private flows.** The overwhelming majority of debt financing in Mexico's balance of payments is from private creditors—debt to official creditor's accounts for about 10 percent of the total external debt stock, and 7 percent of gross flows in 2009.
- **Steady sovereign external access at favorable terms.** Mexico is among the highest-rated emerging markets—notwithstanding last year's rating downgrades by Fitch and S&P's—reflected in a track record of low sovereign external borrowing spreads, including during periods of stress such as during the 2001 recession. While external sovereign spreads have increased since the outbreak of the crisis—as in the case of other highly rated emerging markets—Mexico has retained access at reasonable terms, as demonstrated by the successful placement of US\$1 billion in a 10-year bond deal in January 2010 at a yield of 5¼ percent.
- **Relatively comfortable reserve position.** Mexico's reserves more than cover short-term debt falling due and were viewed as comfortable for normal times before the crisis. Moreover, reserves have been rebuilt to pre-crisis levels of over US\$90 billion. However, since the crisis investors have drawn attention to lower coverage on balance sheet exposures relative to peers and, as discussed in ¶12, it is now believed prudent for reserves to be increased going forward.
- **Sustainable public debt and sound finances.** Fiscal policy is underpinned by the balanced budget rule as well as the authorities' commitment to keep the augmented public sector deficit (including development banks and other levels of government) at a level that stabilizes the overall public debt. Reflecting this, post-crisis projections for public debt and deficits are only somewhat higher (about 2½ and ½ percentage points of GDP, respectively, on average during 2011–13), further supported by the expected stabilization in oil production levels. The staff's DSA analysis discussed in IMF Country Report No. 10/71 shows public debt in Mexico remaining manageable, with public sector gross financing requirements set to continue their trend decline as a share of GDP. No significant contingent liabilities have been incurred thus far in the crisis, with credit guarantees extended by public banks amounting to only about 1 percent of GDP. The authorities' stated medium term agenda includes further efforts to compensate for the projected decline in oil revenues as a share of GDP and to prevent compression of public investment. The authorities have clearly demonstrated their ability to deliver on difficult reforms, passing two major tax reforms since 2007 to begin the process of fiscal consolidation and bringing debt levels down gradually.
- **Low and stable inflation.** Inflation has fallen on a sustained basis in Mexico, including since the introduction of the inflation targeting framework, in the context of a floating exchange rate regime. While headline inflation is rising in 2010, due to the effect of one-off increases in taxes and domestic fuel prices, medium-term inflation expectations have remained well anchored.

- **Absence of systemic bank insolvencies.** The banking system remains liquid and well capitalized. The authorities have moved quickly to address emerging problems in some small institutions, and there are no bank solvency problems that pose an imminent systemic threat. Analysis by Banxico in its 2009 *Financial Stability Report*, and stress tests conducted by staff, show that the system remains well placed to cope with a range of further shocks to credit and market risk.
- **Effective financial sector supervision.** The 2006 FSAP update noted the underlying strength of the regulatory framework and supervisory authorities in Mexico, as well as the substantial progress made since the original FSAP in 2002. Successive Article IV consultations since have echoed these views. The authorities have taken further steps to strengthen the framework for bank resolution and planned to establish a permanent financial stability committee with representatives from the SHCP, Banxico and CNBV. They are also considering tightening the limit on lending by bank subsidiaries based in Mexico to parents abroad, and the disclosure requirement regarding corporates' derivative exposures has also been substantially strengthened.
- **Data transparency and integrity.** The overall quality of Mexican statistics is good, as acknowledged by the 2003 data ROSC. A data ROSC update was conducted in February 2010, and the draft report is being reviewed by the authorities. Mexico has been a subscriber to the SDDS since 1996 and the authorities provide a wealth of data to the public over the internet, with periodicity and timeliness exceeding SDDS requirements in a number of cases. Further measures have been taken to increase the transparency of corporate sector data.

16. ***The authorities' letter (Attachment) highlights their continued commitment to implementing very strong economic policies.*** The authorities note that their policy priorities are to support the ongoing recovery, maintain macroeconomic and financial stability, and continue to lay the basis for strong and sustainable medium term growth. In broad terms, fiscal policy remains anchored by the balanced budget rule and medium term budgetary framework, while monetary policy will remain guided by the inflation targeting framework which has effectively anchored medium-term inflation expectations.

17. ***The policy strategy for the period ahead encompasses the following, as discussed during the 2010 Article IV consultation.***

- **Fiscal policy.** The 2010 budget includes the implementation of a major tax reform to offset the permanent revenue losses from the fall in oil production, along with a temporary easing of the balanced budget rule by $\frac{3}{4}$ percentage point of GDP to cover the cyclical deterioration in tax revenues. As the economy recovers, the authorities plan to return to a balanced budget under the rule by 2012. The authorities are continuing with efforts to restrain and rationalize current expenditure and further

strengthen tax administration, to help offset pressures from rising pension and social expenditures, and finance priority public investment.

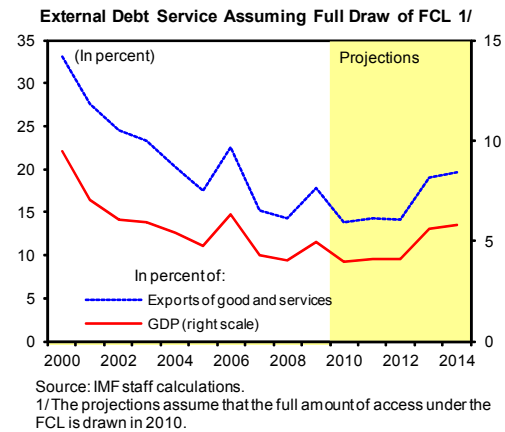
- **Monetary and exchange rate policy.** Monetary policy will remain guided by the inflation targeting framework. The absence of signs of a strong rally in consumption or investment combined with the fiscal consolidation in 2010 argues for a supportive monetary policy stance. The large output gap and the authorities' clear communication strategy should contain second round effects. Nonetheless, Banxico is watching closely the development of expectations. Consistent with the monetary framework, the authorities will also maintain the flexible exchange rate regime, which has proved to be an important shock absorber during the crisis.
- **Financial stability.** Over the last year's, the authorities have moved quickly to address pressures in some small institutions, and manageable risks to the sector are expected to remain. The authorities are planning to widen the regulatory perimeter to better monitor these entities and gather more information on their size, soundness and linkages to the rest of the system. The authorities are also considering establishing a committee of supervisory and regulatory institutions in Mexico to monitor systemic risks, tightening regulations on related party lending by Mexican subsidiaries of foreign banks, and strengthening collaboration with supervisors in other countries.
- **External insurance.** The authorities intend to gradually increase external insurance. This will be achieved through a combination of retaining public sector foreign exchange receipts—mainly from PEMEX—and a rules-based intervention mechanism consistent with the context of the freely floating exchange regime (see IMF Country Report No. 10/71).

III. IMPACT ON FUND FINANCES, RISKS, AND SAFEGUARDS

18. ***Access under the proposed FCL for Mexico of 1,000 percent of quota (SDR 31.528 billion) is large but manageable.*** The Fund's liquidity is expected to remain adequate after the approval of the FCL arrangement for Mexico, as further discussed in the supplement assessing the impact on the Fund's finances and liquidity position.

19. ***Risks to the Fund are expected to be low.*** The authorities have given clear indications that they intend to treat the facility as precautionary. Even if a full drawing under the facility were to be made on approval, Mexico's external debt would remain moderate at

about 27 percent of GDP and at 21 percent of GDP in 2014, when debt service peaks (Table 7). Further, as the Text Chart shows, even peak debt service ratios would be lower than in recent years, and remain well within the range seen in other emerging market countries. Moreover, Mexico has a demonstrated excellent track record of meeting its obligations to the Fund.



20. **Safeguards.** The 2008 audited financial statements and audit information regarding Banxico was provided to staff. There were no material audit findings or significant control or accounting weaknesses identified. The 2009 audit of financial statements has not been completed yet. The authorities have indicated that they will provide authorization for staff to have access to the Banxico’s 2009 external audit report and to hold discussions with the external auditors, as required under the Fund’s safeguards policy for the FCL.

IV. STAFF APPRAISAL

21. **A successor FCL arrangement could continue to play an important role in supporting Mexico’s economic policy strategy.** While Mexico’s underlying fundamentals are very strong, the expiration of the Fed swap line, and the continued risks in the global environment—in the context of Mexico’s large and open capital markets—make a strong case for keeping contingent financing from the Fund in place. A successor FCL arrangement for 1,000 percent of quota—which the authorities intend to treat as precautionary—could continue to play an important role in supporting confidence and the authorities’ economic policy strategy, given still persistent downside risks and the expiration of the Fed swap line which has reduced the availability of contingent insurance.

22. **The staff assesses that Mexico meets the qualification criteria for access to FCL resources and recommends approval of an FCL arrangement for Mexico of SDR 31.528 billion for a period of 12 months.** The authorities have reacted flexibly and appropriately in response to the effects on Mexico of the global financial crisis. Their letter reaffirming a commitment to maintaining such policies in the future, and their track record, provide very strong reassurance that they would react appropriately to any future balance of payments difficulties. Risks to the Fund are contained by the very strong policy setting, the authorities’ intent to treat the FCL arrangement as precautionary, Mexico’s very strong repurchase track record with the Fund, as well as the manageable external debt service profile even if the authorities were to draw the full amount available up-front. Moreover, as explained in ¶15, Mexico meets the qualification criteria for use of FCL resources, which dovetails with the very positive assessment of policies by the Executive Board in the context of the 2010 Article IV consultation with Mexico.

Table 1. Mexico: Selected Economic, Financial, and Social Indicators, 2005–2011

| I. Social and Demographic Indicators | | | | | | | |
|---|-------|-------|-------|-------|--|---------------|---------------|
| GDP per capita (U.S. dollars, 2007) | 9.693 | | | | Households below the poverty line (percent, 2002) | | 33.0 |
| Population (millions, 2007) | 105.8 | | | | Income share of highest 20 percent/lowest 20 percent | | 12.8 |
| Life expectancy at birth (years, 2006) | 74.5 | | | | Adult illiteracy rate (2005) | | 8.4 |
| Under 5 mortality rate (per thousand, 2006) | 35.3 | | | | Gross primary education enrollment rate (2006) | | 112.7 |
| II. Economic Indicators | | | | | | | |
| | 2005 | 2006 | 2007 | 2008 | Prel. 2009 | Proj. 2010 | Proj. 2011 |
| (Annual percentage change, unless otherwise indicated) | | | | | | | |
| National accounts in constant prices | | | | | | | |
| Real GDP | 3.2 | 4.9 | 3.3 | 1.5 | -6.5 | 4.0 | 4.5 |
| Net exports (contribution) | -0.6 | -0.7 | -0.6 | -1.0 | 1.3 | -0.5 | -0.2 |
| Total domestic demand | 3.7 | 5.7 | 3.8 | 2.3 | -7.8 | 4.6 | 4.6 |
| Private consumption | 4.8 | 5.7 | 3.9 | 1.5 | -5.8 | 6.6 | 4.6 |
| Public consumption | 2.4 | 1.7 | 2.1 | 0.6 | 2.4 | -1.8 | 3.7 |
| Gross fixed investment | 7.5 | 9.8 | 7.2 | 4.9 | -12.5 | -1.5 | 3.2 |
| Change in business inventories (contribution) | -1.2 | -0.3 | -0.5 | 0.1 | -1.4 | 0.7 | 0.4 |
| External sector | | | | | | | |
| Exports, f.o.b. | 14.0 | 16.7 | 8.8 | 7.2 | -21.2 | 19.6 | 7.6 |
| Export volume | 5.3 | 8.5 | 3.5 | -2.4 | -11.2 | 10.4 | 4.7 |
| Imports, f.o.b. | 12.7 | 15.4 | 10.1 | 9.5 | -24.0 | 12.1 | 8.8 |
| Import volume | 7.3 | 10.4 | 4.4 | 1.0 | -18.2 | 3.2 | 3.7 |
| Petroleum exports (percent of total exports) | 14.9 | 15.6 | 15.8 | 17.4 | 13.4 | 12.4 | 12.1 |
| Terms of trade (deterioration -) | 3.0 | 2.9 | -0.3 | 1.3 | -11.3 | 0.4 | -0.4 |
| Exchange rates | | | | | | | |
| Nominal exchange rate (US\$/Mex\$) | | | | | | | |
| (average, depreciation -) | 3.4 | 0.0 | -0.3 | -1.8 | -21.4 | ... | ... |
| Real effective exchange rate (CPI based) | | | | | | | |
| (average, depreciation -) | 4.1 | 0.5 | -0.1 | -0.7 | -12.9 | ... | ... |
| Employment and inflation | | | | | | | |
| Consumer prices (end of year) | 3.3 | 4.1 | 3.8 | 6.5 | 3.6 | 5.3 | 3.0 |
| Formal sector employment (annual average) | 3.2 | 4.7 | 4.2 | 2.1 | -3.1 | ... | ... |
| Formal sector unemployment rate (annual average) | 3.6 | 3.6 | 3.7 | 4.0 | 5.5 | 5.0 | 4.5 |
| Real manufacturing wages (annual average) | -0.2 | 0.4 | 1.0 | 0.9 | ... | ... | ... |
| Money and credit | | | | | | | |
| Broad money (M4a) | 15.0 | 12.8 | 11.5 | 17.2 | 5.9 | 6.7 | 9.8 |
| Treasury bill rate (28-day cetes, in percent, annual average) | 9.2 | 7.2 | 7.2 | 7.6 | 5.4 | ... | ... |
| (In percent of GDP) | | | | | | | |
| Nonfinancial public sector | | | | | | | |
| Augmented balance 1/ | -1.4 | -1.0 | -1.4 | -1.5 | -4.7 | -3.4 | -3.0 |
| Augmented primary balance | 1.5 | 1.8 | 1.3 | 1.1 | -2.0 | -1.6 | -0.9 |
| Traditional balance 2/ | -0.1 | 0.1 | 0.0 | -0.1 | -2.3 | -2.7 | -2.3 |
| Gross public sector debt | 39.8 | 38.3 | 38.2 | 43.3 | 44.6 | 44.6 | 44.2 |
| Net public sector debt | 35.2 | 32.4 | 31.4 | 35.8 | 38.8 | 39.1 | 39.0 |
| Savings and investment | | | | | | | |
| Gross domestic investment | 24.4 | 26.1 | 25.8 | 26.4 | 22.1 | 21.9 | 22.5 |
| Public investment | 4.6 | 4.3 | 4.7 | 5.5 | 5.8 | 5.0 | 4.4 |
| Private investment | 15.6 | 16.5 | 16.7 | 16.6 | 15.7 | 14.9 | 15.3 |
| Change in inventories | 4.2 | 5.3 | 4.5 | 4.2 | 0.6 | 1.9 | 2.8 |
| Gross national saving | 23.8 | 25.7 | 25.0 | 24.9 | 21.4 | 20.4 | 20.9 |
| Public saving 3/ | 3.2 | 3.7 | 3.3 | 3.7 | 0.6 | 1.1 | 0.9 |
| Private saving | 20.6 | 22.0 | 21.7 | 21.2 | 20.7 | 19.2 | 20.0 |
| External current account balance | -0.5 | -0.5 | -0.8 | -1.5 | -0.6 | -1.4 | -1.5 |
| Non-oil external current account balance | -2.3 | -2.5 | -2.7 | -3.0 | -1.9 | -2.0 | -1.5 |
| Net foreign direct investment | 1.9 | 1.5 | 2.7 | 2.1 | 1.3 | 2.3 | 2.2 |
| (In percent of exports of goods, nonfactor services, and transfers) | | | | | | | |
| Public external debt service 4/ | 9.4 | 14.3 | 7.5 | 6.8 | 8.8 | 7.3 | 8.1 |
| (In billions of U.S. dollars, unless otherwise indicated) | | | | | | | |
| Net international reserves | 68.7 | 67.7 | 78.0 | 85.4 | 90.8 | 105.8 | 120.8 |
| Gross official reserves in percent of short-term debt 5/ | 111.4 | 147.7 | 153.9 | 165.9 | 208.2 | 209.1 | 187.5 |
| Gross external debt (in percent of GDP, end of period) | 20.4 | 17.8 | 18.8 | 18.5 | 23.8 | 22.7 | 22.9 |
| Crude oil export price, Mexican mix (US\$/bbl) | 42.8 | 53.1 | 61.7 | 84.4 | 57.8 | 70.8 | 74.8 |

Sources: National Institute of Statistics and Geography; Bank of Mexico; Secretariat of Finance and Public Credit; and IMF staff estimates.

1/ Public Sector Borrowing Requirements excl. nonrecurrent revenue.

2/ The break in the series in 2009 is due to definitional and accounting changes.

3/ Estimated as the difference between the augmented fiscal balance, as reported by SHCP, and public investment, as reported in the national accounts.

4/ Debt service on gross external debt of the federal government, development banks and nonfinancial public enterprises (adjusted for Pidiregas).

5/ In percent of short-term debt by residual maturity. Historical data include all prepayments.

Table 2. Mexico: Financial Operations of the Public Sector, 2005–2015
(In percent of GDP)

| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | | 2011 | 2012 | 2013 | 2014 | 2015 |
|--|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | | | | | | Budget | Proj. | Proj. | Proj. | Proj. | Proj. | Proj. |
| Budgetary revenue, by type | 21.1 | 21.8 | 22.2 | 23.6 | 23.6 | 21.9 | 22.0 | 21.8 | 21.7 | 21.6 | 21.3 | 21.1 |
| Oil revenue | 7.9 | 8.3 | 7.9 | 8.7 | 7.9 | 7.1 | 7.0 | 6.7 | 6.5 | 6.4 | 6.3 | 6.2 |
| Non-oil tax revenue 1/ | 8.6 | 9.0 | 9.3 | 10.0 | 9.4 | 10.3 | 10.4 | 10.7 | 10.9 | 10.9 | 10.7 | 10.6 |
| Non-oil non-tax revenue | 4.6 | 4.5 | 5.0 | 4.9 | 6.3 | 4.4 | 4.5 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 |
| Budgetary revenue, by entity | | | | | | | | | | | | |
| Federal government revenue | 15.3 | 15.0 | 15.3 | 16.9 | 16.8 | 15.6 | 15.0 | 14.9 | 14.9 | 14.8 | 14.5 | 14.4 |
| Tax revenue, of which: | 8.8 | 8.6 | 8.9 | 8.2 | 9.5 | 10.2 | 10.6 | 10.9 | 11.2 | 11.2 | 11.2 | 11.1 |
| excises (including fuel) | 0.5 | -0.1 | -0.1 | -1.4 | 0.4 | 0.4 | 0.7 | 0.7 | 0.7 | 0.8 | 0.9 | 0.9 |
| Nontax revenue | 6.5 | 6.4 | 6.3 | 8.7 | 7.3 | 5.3 | 4.4 | 4.0 | 3.7 | 3.6 | 3.4 | 3.3 |
| Public enterprises | 5.8 | 6.8 | 6.9 | 6.7 | 6.8 | 6.3 | 7.0 | 6.9 | 6.8 | 6.8 | 6.8 | 6.8 |
| PEMEX | 2.0 | 3.1 | 3.3 | 3.0 | 3.2 | 2.8 | 3.6 | 3.5 | 3.4 | 3.4 | 3.3 | 3.3 |
| Other | 3.8 | 3.7 | 3.6 | 3.7 | 3.7 | 3.5 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 |
| Budgetary expenditure | 21.2 | 21.7 | 22.2 | 23.7 | 25.9 | 24.6 | 24.7 | 24.0 | 23.7 | 23.6 | 23.3 | 23.1 |
| Primary | 18.9 | 19.3 | 20.0 | 21.8 | 23.7 | 22.3 | 22.4 | 21.7 | 21.3 | 21.1 | 20.8 | 20.5 |
| Programmable | 15.8 | 16.0 | 16.9 | 18.3 | 20.5 | 18.8 | 19.1 | 18.3 | 18.0 | 17.8 | 17.5 | 17.3 |
| Current | 12.7 | 12.7 | 13.3 | 13.9 | 15.3 | 14.2 | 14.1 | 13.9 | 13.8 | 13.7 | 13.7 | 13.7 |
| Wages | 6.0 | 5.9 | 5.8 | 5.9 | 6.4 | 6.3 | 6.1 | 5.9 | 5.7 | 5.5 | 5.3 | 5.2 |
| Pensions | 1.9 | 1.9 | 2.1 | 2.1 | 2.4 | 2.4 | 2.3 | 2.5 | 2.6 | 2.7 | 2.9 | 3.1 |
| Subsidies and transfers | 2.2 | 2.2 | 2.3 | 2.7 | 3.1 | 2.9 | 2.8 | 2.8 | 2.8 | 2.8 | 2.8 | 2.8 |
| Other | 2.5 | 2.8 | 3.1 | 3.2 | 3.4 | 2.6 | 2.8 | 2.8 | 2.8 | 2.7 | 2.7 | 2.6 |
| Capital | 3.1 | 3.2 | 3.6 | 4.4 | 5.1 | 4.6 | 5.0 | 4.4 | 4.2 | 4.1 | 3.8 | 3.6 |
| Physical capital | 2.5 | 2.6 | 2.8 | 3.1 | 4.6 | 4.5 | 4.7 | 4.2 | 4.0 | 3.9 | 3.7 | 3.5 |
| Of which: non Pemex | 2.3 | 2.4 | 2.5 | 2.5 | 2.4 | 2.7 | 2.2 | 2.0 | 1.9 | 1.7 | 1.7 | 1.5 |
| Financial capital | 0.6 | 0.6 | 0.8 | 1.3 | 0.5 | 0.1 | 0.3 | 0.2 | 0.1 | 0.1 | 0.1 | 0.1 |
| Nonprogrammable | 3.1 | 3.4 | 3.1 | 3.6 | 3.3 | 3.6 | 3.3 | 3.3 | 3.4 | 3.3 | 3.3 | 3.2 |
| Of which: revenue sharing | 3.0 | 3.2 | 3.0 | 3.5 | 3.2 | 3.5 | 3.2 | 3.2 | 3.3 | 3.2 | 3.2 | 3.1 |
| Interest payments 2/ | 2.3 | 2.4 | 2.1 | 1.9 | 2.2 | 2.3 | 2.2 | 2.3 | 2.4 | 2.5 | 2.5 | 2.6 |
| Traditional balance 3/ | -0.1 | 0.1 | 0.0 | -0.1 | -2.3 | -2.8 | -2.7 | -2.3 | -2.0 | -2.0 | -2.0 | -2.0 |
| Traditional balance for balanced budget rule | ... | ... | 0.0 | -0.1 | -0.2 | -0.7 | -0.7 | -0.3 | 0.0 | 0.0 | 0.0 | 0.0 |
| Adjustments to the traditional balance | 1.4 | 1.3 | 1.5 | 1.4 | 2.4 | 1.3 | 0.8 | 0.8 | 0.7 | 0.6 | 0.6 | 0.6 |
| PIDIREGAS | 0.8 | 1.1 | 0.9 | 1.1 | 0.0 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| IPAB | 0.2 | 0.1 | 0.1 | 0.2 | 0.1 | 0.2 | 0.2 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| Budgetary adjustments | 0.1 | 0.2 | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.2 | 0.2 | 0.2 | 0.2 |
| PEMEX oil stabilization fund, FARP (-: net inflows) | -0.1 | -0.5 | -0.4 | -1.0 | 0.7 | 0.3 | -0.3 | -0.2 | -0.1 | -0.1 | -0.1 | -0.1 |
| FARAC | 0.0 | 0.0 | -0.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Debtor support | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Development banks (changes in capital) | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Nonrecurring revenue | 0.2 | 0.3 | 0.6 | 0.7 | 1.3 | 0.4 | 0.5 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 |
| Augmented balance (excl. net lending of dev. banks) 4/ | -1.4 | -1.0 | -1.4 | -1.5 | -4.7 | -4.1 | -3.4 | -3.0 | -2.7 | -2.6 | -2.6 | -2.6 |
| Augmented interest expenditure | 2.9 | 2.8 | 2.7 | 2.5 | 2.7 | 2.4 | 2.6 | 2.6 | 2.6 | 2.6 | 2.7 | 2.7 |
| Augmented primary balance (excl. dev. banks) 5/ | 1.5 | 1.8 | 1.3 | 1.1 | -2.0 | -1.6 | -0.9 | -0.5 | -0.1 | 0.0 | 0.0 | 0.1 |
| Memorandum items | | | | | | | | | | | | |
| Crude oil export price, Mexican mix (US\$/bbl) | 42.8 | 53.1 | 61.7 | 84.4 | 57.7 | 59.0 | 70.8 | 74.7 | 75.0 | 76.6 | 78.3 | 80.6 |
| Development banks | -0.1 | -0.5 | 0.0 | 0.4 | 0.4 | 0.5 | 0.5 | 0.4 | 0.3 | 0.3 | 0.3 | 0.3 |
| Augmented balance (incl. net lending of dev. banks) 4/ | -1.3 | -0.6 | -1.4 | -1.8 | -5.1 | -4.5 | -3.9 | -3.4 | -3.0 | -3.0 | -3.0 | -3.0 |
| Augmented primary balance (incl. net lending of dev. banks) 5/ | 1.6 | 2.2 | 1.2 | 0.7 | -2.4 | -2.1 | -1.4 | -0.9 | -0.4 | -0.4 | -0.3 | -0.2 |
| Non-oil augmented balance 6/ | -6.4 | -5.8 | -6.5 | -7.5 | -9.5 | ... | -7.5 | -6.7 | -6.0 | -5.9 | -5.8 | -5.7 |
| Oil augmented balance | 5.0 | 5.2 | 5.0 | 5.7 | 4.3 | ... | 3.6 | 3.3 | 3.0 | 2.9 | 2.8 | 2.7 |
| Gross public sector debt | 39.8 | 38.3 | 38.2 | 43.3 | 44.6 | ... | 44.6 | 44.2 | 43.4 | 42.8 | 42.5 | 42.4 |
| Domestic (percentage of total debt) | 67.9 | 73.5 | 73.0 | 70.3 | 73.1 | ... | 75.5 | 77.3 | 79.0 | 80.3 | 81.6 | 82.9 |
| External (percentage of total debt) | 32.1 | 26.5 | 27.0 | 29.7 | 26.9 | ... | 24.5 | 22.7 | 21.0 | 19.7 | 18.4 | 17.1 |
| Net public sector debt | 35.2 | 32.4 | 31.4 | 35.8 | 38.8 | ... | 39.1 | 39.0 | 38.5 | 38.1 | 38.0 | 38.1 |
| Nominal GDP (billions of Mexican pesos) | 9,252 | 10,382 | 11,208 | 12,131 | 11,823 | 12,793 | 13,171 | 14,337 | 15,591 | 16,885 | 18,175 | 19,470 |

Sources: Mexican authorities; and IMF staff estimates. Data refer to non-financial public sector, including PEMEX and other public enterprises but excluding state and local governments (except as noted).

1/ Total tax revenue excluding excise tax on gasoline.

2/ Includes transfers to IPAB and the debtor support programs.

3/ The break in the series in 2009 is due to definitional and accounting changes.

4/ Public Sector Borrowing Requirements excl. nonrecurrent revenue.

5/ Treats transfers to IPAB as interest payments.

6/ Excludes oil revenue (oil extraction rights, PEMEX net income, oil excess return levies, excise tax on gasoline) and PEMEX operational expenditure, interest payments, and capital expenditure.

Table 3. Mexico: Summary Balance of Payments, 2005–15

| | 2005 | 2006 | 2007 | 2008 | Est. | | Projections | | | | |
|---|---|--------|--------|--------|--------|--------|-------------|--------|--------|--------|--------|
| | | | | | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
| | (In billions of U.S. dollars) | | | | | | | | | | |
| Current account | -4.5 | -4.4 | -8.4 | -15.9 | -5.2 | -14.0 | -15.6 | -19.9 | -19.7 | -19.3 | -19.5 |
| Merchandise trade balance, f.o.b. | -7.6 | -6.1 | -10.1 | -17.3 | -4.7 | -9.1 | -12.4 | -17.5 | -17.5 | -18.1 | -18.9 |
| Exports | 214.2 | 249.9 | 271.9 | 291.3 | 229.7 | 276.2 | 297.5 | 319.7 | 344.8 | 370.8 | 398.3 |
| Imports | -221.8 | -256.1 | -281.9 | -308.6 | -234.4 | -285.3 | -309.9 | -337.2 | -362.3 | -388.9 | -417.2 |
| Factor income | -14.4 | -18.5 | -18.4 | -17.0 | -14.1 | -17.9 | -17.3 | -17.8 | -19.2 | -19.9 | -19.5 |
| Net services | -4.7 | -5.7 | -6.3 | -7.1 | -8.0 | -8.5 | -9.3 | -10.1 | -10.9 | -11.5 | -12.0 |
| Net transfers | 22.1 | 25.9 | 26.4 | 25.5 | 21.5 | 21.5 | 23.5 | 25.6 | 27.9 | 30.2 | 30.9 |
| of which Remittances | 21.7 | 25.6 | 26.1 | 25.1 | 21.2 | 21.2 | 23.1 | 25.2 | 27.5 | 29.7 | 30.4 |
| Financial account | 14.8 | -2.7 | 19.7 | 24.5 | 14.6 | 29.0 | 30.6 | 29.9 | 24.7 | 24.3 | 21.5 |
| Public sector 1/ | 1.4 | -12.5 | 14.1 | 14.9 | 27.3 | 11.4 | -0.1 | 0.7 | 1.8 | 1.8 | 1.8 |
| Medium- and long-term borrowing | -7.3 | -20.5 | -5.1 | -1.1 | 18.2 | 8.2 | -2.5 | -1.9 | -1.0 | -1.0 | -1.0 |
| Disbursements | 6.8 | 9.8 | 6.6 | 10.0 | 29.3 | 17.2 | 11.0 | 11.4 | 12.2 | 12.1 | 12.1 |
| Amortization 2/ | 14.1 | 30.3 | 11.7 | 11.1 | 11.1 | 9.0 | 13.5 | 13.3 | 13.2 | 13.1 | 13.1 |
| Pidiregas, net 3/ | 8.7 | 7.0 | 13.2 | 12.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other, including short-term borrowing and change in assets | 0.0 | 0.9 | 6.0 | 3.1 | 9.1 | 3.2 | 2.4 | 2.6 | 2.8 | 2.8 | 2.8 |
| Of which: oil hedging capital income | ... | ... | ... | ... | 5.1 | ... | ... | ... | ... | ... | ... |
| Private sector | 13.4 | 9.8 | 5.6 | 9.6 | -12.7 | 17.6 | 30.7 | 29.3 | 23.0 | 22.5 | 19.7 |
| Direct investment, net | 15.9 | 14.0 | 19.1 | 22.0 | 3.8 | 17.5 | 18.3 | 19.1 | 20.1 | 20.1 | 20.2 |
| Bonds and loans | 1.9 | 5.2 | 8.8 | -0.9 | -3.7 | 4.3 | 17.1 | 14.5 | 6.9 | 6.4 | 3.5 |
| Equity investments and change in assets abroad | -4.4 | -9.4 | -22.3 | -11.4 | -12.9 | -4.3 | -4.7 | -4.4 | -4.0 | -4.0 | -4.0 |
| Errors and omissions and valuation adjustments | -3.1 | 6.1 | -1.0 | -1.2 | -4.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net international reserves (increase -) | -7.1 | 1.0 | -10.4 | -7.4 | -5.4 | -15.0 | -15.0 | -10.0 | -5.0 | -5.0 | -2.0 |
| | (In percent of GDP, unless otherwise indicated) | | | | | | | | | | |
| Memorandum items: | | | | | | | | | | | |
| Current account balance | -0.5 | -0.5 | -0.8 | -1.5 | -0.6 | -1.4 | -1.5 | -1.7 | -1.6 | -1.5 | -1.4 |
| Nonoil current account balance 4/ | -2.3 | -2.5 | -2.7 | -3.0 | -1.8 | -1.9 | -1.4 | -1.1 | -0.7 | -0.1 | 0.2 |
| Nonoil trade balance 4/ | -2.7 | -2.6 | -2.9 | -3.1 | -1.7 | -1.4 | -1.1 | -0.9 | -0.5 | -0.1 | 0.3 |
| Oil trade balance | 1.8 | 2.0 | 1.9 | 1.5 | 1.2 | 0.5 | 0.0 | -0.6 | -0.9 | -1.3 | -1.6 |
| Gross financing needs (billions of US\$) 4/ | 59.2 | 70.0 | 70.4 | 80.0 | 68.1 | 76.9 | 84.5 | 97.0 | 102.6 | 104.9 | 104.0 |
| Gross international reserves (change, billions of US\$) 5/ | 9.9 | 2.2 | 10.9 | 8.1 | 4.6 | 15.0 | 15.0 | 10.0 | 5.0 | 5.0 | 2.0 |
| End-year (billions of US\$) | 74.1 | 76.3 | 87.2 | 95.3 | 99.9 | 114.9 | 129.9 | 139.9 | 144.9 | 149.9 | 151.9 |
| Months of imports of goods and services | 3.2 | 3.0 | 3.1 | 4.4 | 3.9 | 4.1 | 4.3 | 4.3 | 4.1 | 4.0 | ... |
| Months of imports plus interest payments | 3.4 | 3.1 | 3.3 | 4.7 | 4.1 | 4.3 | 4.5 | 4.5 | 4.3 | 4.1 | ... |
| Percent of short-term debt (by residual maturity) 6/ | 111.4 | 147.7 | 153.9 | 165.9 | 208.3 | 213.4 | 193.7 | 179.6 | 179.8 | 181.7 | ... |
| Gross total external debt | 20.4 | 17.8 | 18.8 | 18.5 | 23.8 | 22.6 | 22.7 | 22.4 | 21.5 | 20.7 | 19.9 |
| Of which: Public external debt | 12.4 | 9.8 | 10.0 | 10.3 | 11.5 | 10.9 | 10.0 | 9.1 | 8.4 | 7.8 | 7.2 |
| Gross total external debt (billions of US\$) | 173.1 | 169.1 | 193.1 | 201.2 | 209.6 | 225.3 | 242.3 | 257.5 | 266.1 | 274.3 | 279.5 |
| Of which: Public external debt 7/ | 104.9 | 93.1 | 102.6 | 112.2 | 100.9 | 109.1 | 106.6 | 104.7 | 103.7 | 102.7 | 101.7 |
| Public external debt service (in percent of exports of goods, services, and transfers) 8/ | 9.4 | 14.3 | 7.5 | 6.8 | 6.7 | 6.0 | 6.9 | 6.8 | 6.5 | 6.0 | 5.4 |

Sources: Bank of Mexico; Secretariat of Finance and Public Credit; and Fund staff projections.

1/ Including the financing of PIDIREGAS.

2/ Includes pre-payment of external debt.

3/ Break in the series in 2009 due to accounting changes.

4/ Excluding oil exports and petroleum products imports.

5/ Excludes balances under bilateral payments accounts. For 2009, includes the allocation of SDR 2.337 billion in the general allocation implemented on August 28, 2009, and another SDR 0.224 billion in the special allocation on September 9.

6/ In percent of short-term debt by residual maturity. Historical data include all prepayments.

7/ Includes gross external debt of the federal government, development banks and nonfinancial public enterprises, and is adjusted for PIDIREGAS.

8/ Includes amortization on medium and long-term bonds and debt, and interest payments.

Table 4. Mexico: External Financing Requirements and Sources, 2005-10
(In billions of U.S. dollars)

| | 2005 | 2006 | 2007 | 2008 | 2009 Est. | 2010 Proj. |
|---|------|-------|-------|-------|--------------|---------------|
| Gross financing requirements | 59.2 | 70.0 | 70.4 | 80.0 | 68.1 | 76.9 |
| Current account deficit | 4.5 | 4.4 | 8.4 | 15.9 | 5.2 | 14.0 |
| Public sector medium and long term amortization 1/ | 16.4 | 33.3 | 15.2 | 14.4 | 11.1 | 9.0 |
| Public sector bonds 2/ | 8.8 | 13.8 | 8.8 | 6.9 | 4.9 | 5.5 |
| Public sector MLT debt | 5.3 | 16.5 | 2.9 | 4.2 | 6.2 | 3.5 |
| PIDIREGAS 3/ | 2.3 | 3.0 | 3.5 | 3.2 | 0.0 | 0.0 |
| Private sector medium and long term amortization 4/ | 11.5 | 12.8 | 13.9 | 15.5 | 20.6 | 16.0 |
| Private sector bonds 4/ | 4.6 | 5.7 | 6.0 | 6.7 | 6.0 | 5.8 |
| Private sector medium and long term debt | 6.9 | 7.1 | 8.0 | 8.8 | 14.7 | 10.2 |
| Short term financing | 19.5 | 20.4 | 22.6 | 26.8 | 25.7 | 22.9 |
| Public sector 2/ | 6.3 | 6.7 | 7.0 | 9.4 | 7.2 | 2.1 |
| Private sector 4/ 5/ | 4.4 | 5.8 | 6.2 | 7.1 | 6.9 | 9.2 |
| Trade credit 6/ | 8.9 | 7.9 | 9.4 | 10.2 | 11.6 | 11.6 |
| Change in international reserves | 7.2 | -1.0 | 10.3 | 7.5 | 5.4 | 15.0 |
| Available financing | 59.2 | 70.0 | 70.4 | 80.0 | 68.1 | 76.9 |
| FDI, net | 15.9 | 14.0 | 19.1 | 22.0 | 3.8 | 17.5 |
| Public sector MLT flows 1/ | 21.3 | 23.5 | 32.3 | 32.9 | 32.9 | 20.4 |
| Public sector bonds 2/ | 2.1 | 3.3 | 3.3 | 3.5 | 11.0 | 8.5 |
| Public sector MLT debt | 4.7 | 6.6 | 3.3 | 6.5 | 18.3 | 8.7 |
| PIDIREGAS 3/ | 11.1 | 10.0 | 16.7 | 16.1 | 0.0 | 0.0 |
| Private sector MLT flows 4/ | 12.3 | 14.9 | 19.8 | 12.6 | 20.2 | 19.0 |
| Private sector bonds | 7.6 | 6.5 | 9.0 | 4.1 | 5.6 | 4.8 |
| Private sector MLT debt | 4.7 | 8.4 | 10.8 | 8.5 | 14.7 | 14.2 |
| Short-term financing | 17.2 | 20.7 | 22.5 | 25.2 | 28.5 | 24.3 |
| Public sector 2/ | 3.5 | 5.1 | 5.2 | 6.6 | 7.7 | 2.1 |
| Private sector 4/ 5/ | 5.8 | 6.2 | 7.1 | 6.9 | 9.2 | 10.6 |
| Trade credit 6/ | 7.9 | 9.4 | 10.2 | 11.6 | 11.6 | 11.6 |
| Other flows | -7.4 | -3.2 | -23.3 | -12.6 | -17.4 | -4.3 |
| of which: | | | | | | |
| Increase in portfolio and other investment assets | -7.7 | -12.2 | -21.8 | -7.9 | -12.0 | -6.0 |
| of which: Oil price hedge | | | | | 5.1 | |

Sources: Mexican authorities and IMF staff estimates.

1/ Including PIDIREGAS.

2/ On a BoP basis.

3/ Includes bonds and loans. For 2003-08, staff estimates based on the stock of debt at original maturity, estimated duration, and net financing data from the Balance of Payments. In 2009, assets from the PEMEX's Master Trust were used to pay down the stock of PIDIREGAS debt.

4/ Gross financing figures for 2003-08 are staff estimates based on data on the stock of debt by residual maturity, estimated duration, and net financing data from the Balance of Payments.

5/ Loans and money market instruments, estimates on original maturity basis.

6/ Includes accounts payable to suppliers and long-term trade credit.

Table 5. Mexico: Gross Public Sector Debt Sustainability Framework, 2005-2015
(In percent of GDP, unless otherwise indicated)

| | Actual | | | | | Projections | | | | | | Debt-stabilizing primary balance 9/ |
|---|--------|-------|-------|-------|-------|-------------|-------------|-------------|-------------|-------------|-------------|---|
| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | |
| 1 Baseline: Gross public sector debt 1/ o/w foreign-currency denominated 7/ | 39.8 | 38.3 | 38.2 | 43.3 | 44.6 | 44.6 | 44.2 | 43.4 | 42.8 | 42.5 | 42.4 | -0.5 |
| | 12.8 | 10.2 | 10.3 | 12.9 | 12.0 | 10.9 | 10.0 | 9.1 | 8.4 | 7.8 | 7.2 | |
| 2 Change in gross public sector debt | -1.6 | -1.5 | -0.1 | 5.2 | 1.2 | 0.0 | -0.4 | -0.8 | -0.6 | -0.3 | -0.1 | |
| 3 Identified debt-creating flows (4+7+12) | -2.6 | -3.8 | -2.0 | 1.0 | 3.4 | -0.8 | -0.6 | -1.0 | -0.8 | -0.5 | -0.3 | |
| 4 Primary deficit | -1.6 | -2.2 | -1.2 | -0.9 | 1.9 | 1.4 | 0.9 | 0.4 | 0.4 | 0.3 | 0.2 | |
| 5 Revenue and grants | 20.8 | 21.4 | 21.4 | 22.9 | 22.3 | 21.4 | 21.3 | 21.3 | 21.1 | 20.9 | 20.7 | |
| 6 Primary (noninterest) expenditure | 19.2 | 19.2 | 20.2 | 22.0 | 24.1 | 22.8 | 22.2 | 21.7 | 21.5 | 21.2 | 20.9 | |
| 7 Automatic debt dynamics 2/ | -0.8 | -1.3 | -0.1 | 2.6 | 2.8 | -1.7 | -1.0 | -1.0 | -0.7 | -0.4 | -0.1 | |
| 8 Contribution from interest rate/growth differential 3/ | -0.1 | -1.6 | -0.2 | -0.1 | 4.0 | -1.7 | -1.0 | -1.0 | -0.7 | -0.4 | -0.1 | |
| 9 Of which contribution from real interest rate | 1.1 | 0.3 | 1.0 | 0.3 | 1.1 | -0.1 | 0.8 | 1.1 | 1.3 | 1.4 | 1.5 | |
| 10 Of which contribution from real GDP growth | -1.2 | -1.8 | -1.2 | -0.5 | 2.9 | -1.6 | -1.8 | -2.1 | -2.0 | -1.7 | -1.6 | |
| 11 Contribution from exchange rate depreciation 4/ | -0.7 | 0.2 | 0.1 | 2.8 | -1.2 | ... | ... | ... | ... | ... | ... | |
| 12 Other identified debt-creating flows | -0.2 | -0.3 | -0.6 | -0.7 | -1.3 | -0.5 | -0.4 | -0.4 | -0.4 | -0.4 | -0.4 | |
| 13 Privatization receipts (negative) | -0.2 | -0.3 | -0.6 | -0.7 | -1.3 | -0.5 | -0.4 | -0.4 | -0.4 | -0.4 | -0.4 | |
| 14 Recognition of implicit or contingent liabilities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| 15 Other (specify, e.g. bank recapitalization) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| 16 Residual, including asset changes (2-3) 5/ | 1.0 | 2.3 | 1.8 | 4.2 | -2.1 | 0.9 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | |
| Gross public sector debt-to-revenue ratio 1/ | 191.3 | 179.1 | 178.4 | 189.3 | 200.3 | 207.9 | 207.4 | 203.8 | 202.7 | 203.7 | 204.6 | |
| Gross financing need 6/ in billions of U.S. dollars | 10.3 | 7.7 | 8.1 | 11.4 | 15.7 | 13.0 | 12.2 | 10.8 | 10.7 | 10.5 | 10.3 | |
| | 87.8 | 73.4 | 83.1 | 123.9 | 138.4 | 129.5 | 130.7 | 124.4 | 132.5 | 138.5 | 144.5 | |
| Scenario with key variables at their historical averages 7/ Scenario with no policy change (constant primary balance) in 2010-2015 | | | | | | 44.6 | 43.2 | 41.8 | 40.3 | 38.9 | 37.4 | -0.8 |
| | | | | | | 44.6 | 43.9 | 44.0 | 44.5 | 45.2 | 46.2 | -0.5 |
| Key Macroeconomic and Fiscal Assumptions Underlying Baseline | | | | | | | | | | | | |
| Real GDP growth (in percent) | 3.2 | 5.1 | 3.3 | 1.3 | -6.6 | 4.0 | 4.5 | 5.2 | 4.9 | 4.4 | 4.0 | |
| Average nominal interest rate on public debt (in percent) 8/ | 7.6 | 7.8 | 7.5 | 7.7 | 7.4 | 6.3 | 6.3 | 6.3 | 6.5 | 6.7 | 6.9 | |
| Average real interest rate (nominal rate minus change in GDP deflator, in p | 3.0 | 1.1 | 3.0 | 1.0 | 2.1 | 0.1 | 2.2 | 2.9 | 3.3 | 3.6 | 3.8 | |
| Nominal appreciation (increase in US dollar value of local currency, in perc | 4.8 | -1.6 | -1.0 | -21.1 | 8.9 | ... | ... | ... | ... | ... | ... | |
| Inflation rate (GDP deflator, in percent) | 4.6 | 6.7 | 4.5 | 6.6 | 5.3 | 6.3 | 4.1 | 3.4 | 3.3 | 3.1 | 3.1 | |
| Growth of real primary spending (deflated by GDP deflator, in percent) | 9.6 | 5.1 | 8.3 | 10.6 | 2.5 | -1.7 | 1.6 | 3.0 | 3.7 | 2.9 | 2.8 | |
| Primary deficit | -1.6 | -2.2 | -1.2 | -0.9 | 1.9 | 1.4 | 0.9 | 0.4 | 0.4 | 0.3 | 0.2 | |

1/ Public sector includes federal government, Pemex, and other public companies, development banks, Pidiregas, IPAB, debtor's program, and Farac.

2/ Derived as $[(r - \pi(1+g) - g + \alpha d(1+r))/(1+g+\pi+g\pi)]$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and d = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as $-g$.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha d(1+r)$.

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 6. Mexico: External Debt Sustainability Framework, 2005-15
(In percent of GDP, unless otherwise indicated)

| | Actual | | | | | Projections | | | | | | Debt-stabilizing non-interest current account 7/ -1.8 |
|---|--------|------|------|------|-------|-------------|------|------|------|------|-------|--|
| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | |
| 1 Baseline: External debt | 20.4 | 17.8 | 18.8 | 18.5 | 23.8 | 22.6 | 22.7 | 22.4 | 21.5 | 20.7 | 19.9 | |
| 2 Change in external debt | -1.5 | -2.6 | 1.1 | -0.3 | 5.3 | -1.2 | 0.1 | -0.4 | -0.9 | -0.8 | -0.9 | |
| 3 Identified external debt-creating flows (4+8+9) | -3.9 | -3.5 | -2.5 | -0.8 | 3.6 | -1.2 | -1.4 | -1.3 | -1.3 | -1.2 | -1.1 | |
| 4 Current account deficit, excluding interest payments | -0.9 | -1.0 | -0.6 | 0.1 | -0.7 | 0.0 | 0.1 | 0.4 | 0.2 | 0.1 | 0.2 | |
| 5 Deficit in balance of goods and services | 1.4 | 1.2 | 1.6 | 2.2 | 1.4 | 1.8 | 2.0 | 2.4 | 2.3 | 2.2 | 2.2 | |
| 6 Exports | 27.1 | 27.9 | 28.2 | 28.4 | 27.8 | 29.2 | 29.4 | 29.3 | 29.4 | 29.5 | 29.8 | |
| 7 Imports | 28.6 | 29.2 | 29.8 | 30.7 | 29.2 | 31.0 | 31.5 | 31.7 | 31.6 | 31.8 | 32.0 | |
| 8 Net non-debt creating capital inflows (negative) | -2.2 | -1.7 | -2.1 | -1.1 | -1.3 | -1.8 | -1.9 | -1.9 | -1.9 | -1.8 | -1.7 | |
| 9 Automatic debt dynamics 1/ | -0.9 | -0.7 | 0.2 | 0.3 | 5.7 | 0.6 | 0.4 | 0.3 | 0.4 | 0.4 | 0.4 | |
| 10 Contribution from nominal interest rate | 1.4 | 1.5 | 1.4 | 1.3 | 1.3 | 1.4 | 1.3 | 1.3 | 1.4 | 1.3 | 1.2 | |
| 11 Contribution from real GDP growth | -0.6 | -0.9 | -0.5 | -0.2 | 1.5 | -0.8 | -0.9 | -1.1 | -1.0 | -0.9 | -0.8 | |
| 12 Contribution from price and exchange rate changes 2/ | -1.7 | -1.3 | -0.7 | -0.8 | 2.9 | ... | ... | ... | ... | ... | ... | |
| 13 Residual, incl. change in gross foreign assets (2-3) 3/ | 2.4 | 0.8 | 3.6 | 0.4 | 1.7 | 0.0 | 1.5 | 0.9 | 0.4 | 0.4 | 0.2 | |
| External debt-to-exports ratio (in percent) | 75.2 | 63.5 | 66.7 | 65.0 | 85.7 | 77.2 | 77.2 | 76.4 | 73.2 | 70.2 | 66.6 | |
| Gross external financing need (in billions of US dollars) 4/ in percent of GDP | 52.0 | 71.0 | 60.1 | 72.6 | 62.7 | 61.9 | 69.5 | 87.0 | 97.6 | 99.9 | 102.0 | |
| | 6.1 | 7.5 | 5.9 | 6.7 | 7.1 | 6.2 | 6.5 | 7.6 | 7.9 | 7.5 | 7.2 | |
| Scenario with key variables at their historical averages 5/ | | | | | | 22.6 | 22.7 | 22.3 | 21.4 | 20.5 | 19.3 | -1.7 |
| Key Macroeconomic Assumptions Underlying Baseline | | | | | | | | | | | | |
| Real GDP growth (in percent) | 3.2 | 5.1 | 3.3 | 1.3 | -6.6 | 4.0 | 4.5 | 5.2 | 4.9 | 4.4 | 4.0 | |
| GDP deflator in US dollars (change in percent) | 8.3 | 6.7 | 4.2 | 4.7 | -13.4 | 8.8 | 2.3 | 2.6 | 2.5 | 2.4 | 2.3 | |
| Nominal external interest rate (in percent) | 7.4 | 8.1 | 8.8 | 7.5 | 5.9 | 6.8 | 6.3 | 6.4 | 6.8 | 6.6 | 6.0 | |
| Growth of exports (US dollar terms, in percent) 6/ | 14.0 | 15.6 | 8.7 | 6.9 | -21.0 | 19.4 | 7.5 | 7.4 | 7.8 | 7.5 | 7.4 | |
| Growth of imports (US dollar terms, in percent) 6/ | 12.6 | 14.6 | 10.0 | 9.2 | -22.9 | 20.3 | 8.4 | 8.7 | 7.4 | 7.3 | 7.2 | |
| Current account balance, excluding interest payments | 0.9 | 1.0 | 0.6 | -0.1 | 0.7 | 0.0 | -0.1 | -0.4 | -0.2 | -0.1 | -0.2 | |
| Net non-debt creating capital inflows | 2.2 | 1.7 | 2.1 | 1.1 | 1.3 | 1.8 | 1.9 | 1.9 | 1.9 | 1.8 | 1.7 | |

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+\tau)] / (1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, ε = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+\tau)] / (1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Goods and nonfactor services.

7/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Table 7. Mexico: Indicators of Fund Credit 2009-2015

| | 2009 | Projections | | | | | 2015 |
|---|------|-------------|--------|--------|--------|--------|-------|
| | | 2010 | 2011 | 2012 | 2013 | 2014 | |
| Stocks from prospective drawings 1/ | | | | | | | |
| Fund credit in millions SDR | 0 | 31,528 | 31,528 | 31,528 | 19,705 | 3,941 | 0 |
| In percent of quota | 0 | 1,000 | 1,000 | 1,000 | 625 | 125 | 0 |
| In percent of GDP | 0 | 5 | 5 | 4 | 2 | 0 | 0 |
| In percent of exports of goods and services | 0 | 17 | 15 | 14 | 8 | 2 | 0 |
| In percent of gross reserves | 0 | 30 | 27 | 26 | 17 | 4 | 0 |
| Flows from prospective drawings 2/ | | | | | | | |
| Charges (Millions SDR) | 0 | 664 | 836 | 836 | 893 | 406 | 27 |
| Debt Service due on GRA credit (Millions SDR) | 0 | 664 | 836 | 836 | 12,716 | 16,170 | 3,968 |
| In percent of quota | 0 | 21 | 27 | 27 | 403 | 513 | 126 |
| In percent of GDP | 0 | 0.1 | 0.1 | 0.1 | 1.6 | 1.9 | 0.4 |
| In percent of exports of goods and services | 0 | 0.3 | 0.4 | 0.4 | 5.3 | 6.3 | 1.4 |
| In percent of gross reserves | 0 | 1 | 1 | 1 | 11 | 16 | 4 |
| Memo Item: | | | | | | | |
| Total External Debt (percent of GDP) | 24 | 27 | 27 | 27 | 24 | 21 | 20 |

Sources: IMF Finance Department; Mexican authorities, and Fund staff estimates

1/ End of period. Assumes full drawings under the FCL upon approval of the arrangement. The Mexican authorities have expressed their intention to treat the arrangement as precautionary. At an SDR/US\$ rate of 0.654169 as of March 10, 2010.

2/ Based on the rate of charge as of March 10, 2010. Includes surcharges under the system currently in force and service charges.

Mexico City, March 10, 2010

Dear Mr. Strauss-Kahn,

Despite the severity of the global financial crisis, exacerbated by the AH1N1 crisis in the second quarter of 2009, economic stability has been maintained in Mexico and economic recovery is now clearly under way. As noted in the recent Article IV consultation paper, this was mainly due to Mexico's strong policy framework and the substantial improvement in public and private sector balance sheets in recent years, aided by the countercyclical policy response. The Flexible Credit Line (FCL) arrangement with the Fund, approved in April 2009, as well as the swap line with the U.S. Federal Reserve, among other extraordinary actions, also played a very important role in supporting our economic strategy and provided confidence to its sustainability.

While the near term outlook for Mexico is favorable, the external environment—as discussed in the recent World Economic Outlook and GFSR Updates—continues to pose substantial risks. Against this background, and in accordance with the decision reached by the Exchange Commission on February 18th, we would like the Fund to approve a successor 12-month FCL arrangement for Mexico in the amount of SDR 31.528 billion (1,000 percent quota). We believe that a successor arrangement, which we again intend to treat as precautionary, could continue to play an important role in supporting our policy strategy, providing insurance against tail risk events, and helping to ensure that public confidence is not compromised.

Over the coming year, our policy priorities are to support the ongoing recovery; maintain macroeconomic and financial stability; and continue to lay the basis for strong and sustainable medium term growth. On the fiscal side, policy remains anchored by our balanced budget rule and medium term budgetary framework.¹ Last year, fiscal policy was able to deliver a sizable countercyclical impulse—estimated at over 2 percent of GDP—to support the economy. The 2010 budget included the implementation of a major tax reform to offset the permanent revenue losses from declining oil production, along with a temporary easing of the balanced budget rule by $\frac{3}{4}$ percentage point of GDP to cover the cyclical deterioration in tax revenues. This will provide an appropriate balance between the twin imperatives of supporting the recovery assuring medium term fiscal sustainability, and will ensure that public debt as a share of GDP is firmly on a downward path. Looking forward, we are continuing our efforts to restrain current expenditure and further strengthen tax administration, to help offset pressures from rising pension and social expenditures, and finance priority public investment.

¹ See http://www.apartados.hacienda.gob.mx/presupuesto/temas/pppf/2010/temas/expo_motivos/criterios/cgpe_2010.pdf.

Monetary policy will remain guided by our inflation targeting framework, which has effectively anchored medium-term inflation expectations. Since late 2008, and in response to the slowdown in the economy and the high output gap, overnight funding rates were lowered by 375 basis points to 4.5 percent. In the meantime, headline inflation fell to 3.57 percent at end-2009. While headline inflation is expected to rise during 2010, mainly reflecting the once-off effect of tax and administrative price measures in the budget, inflation expectations remain well anchored, and inflation is expected to return to the 3 percent target by end-2011, in line with our monetary policy horizon (as discussed in our recent policy statements).² Consistent with our monetary framework, we will also maintain our flexible exchange rate regime, which proved to be an important shock absorber during the crisis. Most recently, a rules based mechanism that will contribute to increase the level of international reserves was also introduced. The latter will provide additional insurance, particularly if one acknowledges that Mexico's reserves are lower in a number of key dimensions than those in many of its emerging market peers. The expected reserve accumulation will be achieved through a combination of purchases of foreign exchange from PEMEX and the Federal Government, and the rules-based mechanism previously mentioned, which is consistent with the free floating exchange rate regime.³

The banking sector remains well capitalized and profitable with healthy prudential ratios, aided by a strong regulatory framework. Over the last year, we moved quickly to address pressures in some small housing finance institutions (SOFOLES), and risks to the sector are expected to remain manageable (as discussed in Banxico's latest recent Financial Stability Report⁴). Development banks have also contributed to provide stability in key market segments and support credit extension in certain sectors. We continue to work in strengthening financial regulation and supervision taking into account ongoing work in the FSB, including through; improving the regulatory framework for non banks, and strengthening collaboration with supervisors in other countries.

² See <http://www.banxico.org.mx/publicaciones-y-discursos/publicaciones/informes-periodicos/trimestral-inflacion/{2303131F-F72D-1284-E524-1E506B0E7DD2}.pdf> .

³ See http://www.hacienda.gob.mx/SALAPRENSA/doc_comunicados_prensa/2010/febrero/shcp_banxico_anuncio_comision_cambios_22feb10.pdf .

⁴ See <http://www.banxico.org.mx/publicaciones-y-discursos/publicaciones/informes-periodicos/reporte-sf/{5286741D-A39E-9745-B393-AF3DF0A5AE85}.pdf> .

Overall, as Executive Directors acknowledged in the recent Article IV consultation discussion, Mexico's economic framework remains strong and economic policies have responded in a timely and appropriate fashion in addressing pressures from the global economic situation, and we will continue to react as needed to any future shocks that may arise.

Sincerely yours,

/s/

Ernesto Javier Cordero Arroyo
Minister of Finance and Public Credit

/s/

Agustín Guillermo Carstens Carstens
Governor of Banco de México

INTERNATIONAL MONETARY FUND

Mexico—Assessment of the Impact of the Proposed Flexible Credit Line Arrangement on the Fund’s Finances and Liquidity Position

Prepared by the Finance and Strategy, Policy and Review Departments

(In consultation with other Departments)

Approved by Andrew Tweedie and Aasim Husain

March 17, 2010

1. **This note assesses the impact of the proposed Flexible Credit Line (FCL) arrangement for Mexico on the Fund’s finances and liquidity position, in accordance with the policy on the FCL arrangements.**¹ The proposed arrangement could cover a 12-month period, and be in an amount of SDR 31.528 billion (1,000 percent of quota) and would succeed the existing FCL arrangement of an identical amount that would be cancelled upon approval of the proposed arrangement. The full amount of access proposed would be available throughout the arrangement period, in one or multiple purchases.² The authorities intend to treat the arrangement as precautionary.

I. BACKGROUND

2. **Against the backdrop of a global economic and financial crisis, a one-year precautionary FCL arrangement equivalent to SDR 31.5 billion was approved on April 17, 2009.** The authorities’ forceful and broad-based policy responses to the effects on Mexico of the global crisis have been successful in maintaining stability, and no drawings have been made under the existing FCL arrangement. As discussed in Annex I, Mexico has a history of strong performance also under earlier Fund arrangements and an exemplary record of meeting its obligations to the Fund.

3. **Total external and public debt levels are moderate.** External debt, which was stable below 20 percent of GDP in the years preceding the recent crisis, increased in 2009 to about 24 percent of GDP owing to the effects of the depreciation of the peso and the significant contraction in real GDP. However, with the recovery in growth, external debt is

¹ See *GRA Lending Toolkit and Conditionality—Reform Proposals* (3/13/09) and *Flexible Credit Line (FCL) Arrangements*, Decision No.14283-(09/29), adopted March 24, 2009.

² If the full amount is not drawn in the first six months of the arrangement, subsequent purchases are subject to a review of Mexico’s continued qualification for the FCL arrangement.

projected to decline to around 20 percent of GDP over the medium term. Short-term debt on a residual maturity basis accounts for about one-quarter of total external debt. Gross public debt that had stabilized at just under 40 percent of GDP before the crisis, is projected to increase to around 45 percent of GDP by end-2010, and to decline slightly in the coming years. Public external debt is estimated at about 11 percent of GDP at end 2010. Sustainability analyses show both external and public debt remaining manageable under a range of scenarios, with no significant contingent liabilities incurred during the crisis.³

4. **Access under the proposed arrangement would be equal to the largest Fund commitment to date and it could result in a record credit exposure.**⁴ The proposed FCL arrangement is equal in size to the largest General Resources Account (GRA) arrangement in the Fund's history, i.e., the existing FCL arrangement for Mexico. If the full amount available under the FCL arrangement—which the authorities intend to treat as precautionary—were drawn, Mexico's outstanding use of GRA resources would reach SDR 31.5 billion, one-third higher than the Fund's largest credit exposure to date.

5. **In case the full amount available under the proposed FCL arrangement is disbursed in 2010:**

- **Mexico's external debt would remain moderate, with Fund credit representing a significant part of this debt:** total external debt would rise to over 27 percent of GDP initially, and public external debt would rise close to 16 percent of GDP, with Fund credit being close to 5 percent of GDP (Table 1). At its peak, Mexico's outstanding use of GRA resources would account for close to 18 percent of total external debt, 32 percent of public external debt, and 30 percent of gross international reserves.
- **External debt service would be substantially higher in the medium-term, but this would likely be manageable assuming a continued recovery in the operation of international financial markets.** Mexico's projected debt service to the Fund would peak in 2014 at about SDR 16.2 billion, or close to 2 percent of GDP.⁵ In terms of exports of goods and services, external debt service to the Fund would peak at close to 6½ percent, accounting for slightly over 60 percent of total public external debt service, which would increase to just over 10 percent of exports of goods and services.

³ A more detailed description of external and public debt is provided in the staff report.

⁴ The largest GRA credit exposure has been SDR 23.359 billion to Brazil in 2003.

⁵ The figures on debt service used in this report are calculated assuming that full amount available under the arrangement is purchased upon approval of the arrangement, and that all repurchases are made as scheduled.

Table 1. Mexico: Capacity to Repay Indicators 1/

| | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
|--|-------|-----------|-----------|-----------|----------|----------|---------|
| Exposure and Repayments (In SDR millions) | | | | | | | |
| GRA credit to Mexico | -- | 31,528.0 | 31,528.0 | 31,528.0 | 19,705.0 | 3,941.0 | -- |
| (In percent of quota) | -- | (1,000.0) | (1,000.0) | (1,000.0) | (625.0) | (125.0) | (0.0) |
| Charges due on GRA credit 2/ | -- | 663.7 | 835.7 | 836.1 | 892.8 | 405.9 | 26.9 |
| Debt service due on GRA credit 2/ | -- | 663.7 | 835.7 | 836.1 | 12,715.8 | 16,169.9 | 3,967.9 |
| Debt and Debt Service Ratios 3/ | | | | | | | |
| In percent of GDP | | | | | | | |
| Total external debt | 23.8 | 27.4 | 27.2 | 26.5 | 23.9 | 21.2 | 19.9 |
| Public external debt | 11.5 | 15.8 | 14.5 | 13.3 | 10.8 | 8.2 | 7.2 |
| GRA credit to Mexico | -- | 4.8 | 4.5 | 4.2 | 2.4 | 0.5 | -- |
| Total external debt service | | | | | | | |
| | 6.5 | 4.9 | 5.2 | 5.9 | 7.9 | 8.0 | 6.3 |
| Public external debt service | 2.1 | 1.2 | 1.6 | 1.5 | 2.8 | 3.0 | 1.5 |
| Debt service due on GRA credit | -- | 0.1 | 0.1 | 0.1 | 1.6 | 1.9 | 0.4 |
| In percent of Gross International Reserves | | | | | | | |
| Total external debt | 209.8 | 167.7 | 163.1 | 162.5 | 169.3 | 179.8 | 184.0 |
| Public external debt | 101.0 | 96.5 | 86.9 | 81.3 | 76.5 | 69.7 | 67.0 |
| GRA credit to Mexico | -- | 29.6 | 27.1 | 25.6 | 17.2 | 3.9 | -- |
| In percent of Exports of Goods and Services | | | | | | | |
| Total external debt service | 23.5 | 16.8 | 17.6 | 20.3 | 26.8 | 27.0 | 21.1 |
| Public external debt service | 7.5 | 4.1 | 5.4 | 5.0 | 9.5 | 10.2 | 5.1 |
| Debt service due on GRA credit | -- | 0.3 | 0.4 | 0.4 | 5.3 | 6.3 | 1.4 |
| In percent of Total External Debt | | | | | | | |
| GRA credit to Mexico | -- | 17.6 | 16.6 | 15.8 | 10.2 | 2.1 | -- |
| In percent of Public External Debt | | | | | | | |
| GRA credit to Mexico | -- | 30.6 | 31.1 | 31.5 | 22.5 | 5.5 | -- |

Sources: Mexican authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ Assumes full drawings under the FCL upon approval. The Mexican authorities have expressed their intention to treat the arrangement as precautionary, as balance of payments pressures have not materialized.

2/ Based on the rate of charge as of March 10, 2010. Includes surcharges under the system currently in force and service charges.

3/ Staff projections for external debt, GDP, gross international reserves, and exports of goods and services, as used in the staff report that requests the proposed FCL, adjusted for the impact of the assumed FCL drawing.

6. Reflecting the very high access under the arrangement, the impact on the Fund's liquidity, and on its potential exposure to credit risk, would be very substantial:

- The proposed arrangement would reduce the Fund's one-year forward commitment capacity (FCC) by about one-sixth.** The liquidity impact of the proposed arrangement would initially be offset by the cancellation of the existing FCL arrangement. In the absence of a new arrangement, however, the FCC would have increased by SDR 31.5 billion at the expiration of the existing FCL arrangement in mid-April (Table 2). The availability of supplementary resources under the bilateral borrowing and note purchase agreements greatly bolsters the Fund's resources and thus mitigates the relative impact that the proposed arrangement would have on the Fund's liquidity position.
- If the resources available under the FCL arrangement were fully drawn, GRA credit to Mexico as a share of total GRA credit would be about 44 percent.** As a

result, the concentration of Fund credit among the top five users of Fund resources would increase moderately to about 83 percent, from 80 percent currently.

- **Potential GRA exposure to Mexico would be very large in relation to the current level of the Fund’s precautionary balances.** If the resources available under the arrangement were fully drawn, Fund credit to Mexico would be equivalent to some 4½ times the Fund’s current precautionary balances.

Table 2. FCL Arrangement for Mexico—Impact on GRA Finances
(In SDR millions, unless otherwise indicated)

| | As of 03/05/10 |
|--|----------------|
| Liquidity measures | |
| Current one-year Forward Commitment Capacity (FCC) 1/ | 155,709 |
| Impact on FCC on approval of FCL 2/ | 31,528 |
| Prudential measures, assuming full FCL drawing | |
| Fund credit to Mexico | |
| In percent of total GRA credit outstanding 3/ | 44.0 |
| In percent of current precautionary balances | 444.5 |
| Fund credit outstanding to five largest debtors | |
| In percent of total GRA credit outstanding, before approval | 80.3 |
| In percent of total GRA credit outstanding, upon approval of the FCL 3/ | 83.1 |
| Memorandum items | |
| Current precautionary balances (end-April 2009) | 7,093 |
| Total FCL commitments, including proposed FCL 4/ | 52,184 |
| Quota of FTP members with actual and proposed FCLs, in percent of total quota of FTP members | 2.9 |

Sources: Finance Department.

1/ The FCC measures the Fund’s capacity to make new credit commitments over the next 12 months. It includes the liquidity effects of resources made available under borrowing and note purchase agreements.

2/ The liquidity impact would fully offset the increase in the FCC resulting from the cancellation of Mexico’s current FCL of the identical size, i.e., the reported FCC would remain unchanged.

3/ Based on current Fund credit outstanding plus full drawings under the proposed FCL.

4/ Excluding Mexico’s existing FCL.

II. ASSESSMENT

7. **The proposed record high commitment has a very substantial, but manageable impact on the Fund’s liquidity.** The current liquidity position is sufficiently strong to accommodate the liquidity impact of the proposed arrangement, in particular as the proposed cancellation of Mexico’s existing FCL arrangement would fully offset the initial reduction in FCC arising from the proposed FCL arrangement. However, the liquidity position could change quickly, particularly if there is further demand for large arrangements. This underscores the need for continued close monitoring of liquidity, and to continue the efforts to bring new borrowing agreements on line to supplement the Fund’s resources.

8. **Mexico intends to treat the FCL arrangement as precautionary, but if it did prove necessary to draw, this would become the Fund’s largest single credit exposure.** Mexico’s overall external debt and debt service ratios are expected to remain moderate even

with a drawing under the arrangement. Hence, given Mexico's sustained track record of implementing very strong policies, including during the global financial crisis, and commitment to maintaining such policies in future, Mexico's capacity to repay is projected to remain strong. Nonetheless, the scale of the Fund's potential exposure to Mexico—in conjunction with the recent increase in lending to other members and the prospects for further credit expansion under already existing or possible new Fund arrangements—underscores the need to strengthen the Fund's precautionary balances.

ANNEX I. MEXICO: HISTORY OF IMF ARRANGEMENTS

This annex provides a brief overview of Mexico's Fund arrangements from 1983 to present.

Prior to the one-year precautionary FCL arrangement approved in April 2009, Mexico had several Fund arrangements in the 1980s and 1990s until it extinguished its remaining outstanding credit in 2000 (Table I.1). Mexico has an exemplary track record of meeting its obligations to the Fund.

From 1983 to 2000, Mexico had two arrangements under the Extended Fund Facility (EFF) and three Stand-By Arrangements (SBAs). Below is a brief description of the two most recent SBAs:

- In February 1995, the Fund approved an SBA equivalent to SDR 12.1 billion (688 percent of quota) to support Mexico's adjustment program to deal with a major financial and economic crisis. Under that arrangement, Mexico made purchases totaling SDR 8.8 billion, and its outstanding credit peaked at SDR 10.6 billion (607 percent of quota) at end-1995 (Figure I.1). After regaining access to international capital markets in the second half of 1996, Mexico made sizable advance repurchases.
- In July 1999, an SBA equivalent to SDR 3.1 billion was approved as the recovery in economic performance was disrupted by unsettled conditions in international capital markets. Solid performance under the program supported by this SBA allowed Mexico to extinguish all its outstanding obligations to the Fund through a series of advance repurchases before the SBA expired in November 2000.

Against the backdrop of a global economic and financial crisis, a one-year precautionary FCL arrangement equivalent to SDR 31.5 billion was approved on April 17, 2009. The authorities' forceful and broad-based policy responses to the effects on Mexico of the global crisis have been successful in maintaining stability and no drawings have been made under the existing FCL arrangement.

Table I.1. Mexico: IMF Financial Arrangements, 1983–2010
(In millions of SDR)

| Year | Type of Arrangement | Date of Arrangement | Date of Expiration or Cancellation | Amount of New Arrangement | Amount Drawn | Purchases | Repurchases | Fund Exposure 1/ |
|------|---------------------|---------------------|------------------------------------|---------------------------|--------------|-----------|-------------|------------------|
| 1983 | EFF | 1-Jan-83 | 31-Dec-85 | 3,410.6 | 2,502.7 | 1,003.1 | 0.0 | 1,203.8 |
| 1984 | | | | | | 1,203.8 | 0.0 | 2,407.5 |
| 1985 | | | | | | 295.8 | 0.0 | 2,703.3 |
| 1986 | SBA | 19-Nov-86 | 1-Apr-88 | 1,400.0 | 1,400.0 | 741.4 2/ | 125.4 | 3,319.3 |
| 1987 | | | | | | 600.0 | 280.0 | 3,639.3 |
| 1988 | | | | | | 350.0 | 419.0 | 3,570.3 |
| 1989 | EFF | 26-May-89 | 25-May-93 | 3,729.6 | 3,263.4 | 943.0 3/ | 639.6 | 3,873.6 |
| 1990 | | | | | | 1,608.4 | 877.1 | 4,604.9 |
| 1991 | | | | | | 932.4 | 807.4 | 4,729.9 |
| 1992 | | | | | | 233.1 | 636.1 | 4,327.0 |
| 1993 | | | | | | 0.0 | 841.7 | 3,485.2 |
| 1994 | | | | | | 0.0 | 841.0 | 2,644.2 |
| 1995 | SBA | 1-Feb-95 | 15-Feb-97 | 12,070.2 | 8,758.0 | 8,758.0 | 754.1 | 10,648.1 |
| 1996 | | | | | | 0.0 | 1,413.6 | 9,234.5 |
| 1997 | | | | | | 0.0 | 2,499.2 | 6,735.2 |
| 1998 | | | | | | 0.0 | 783.7 | 5,951.5 |
| 1999 | SBA | 07-Jul-1999 | 30-Nov-2000 | 3,103.0 | 1,939.5 | 1,034.4 | 3,726.7 | 3,259.2 |
| 2000 | | | | | | 905.1 | 4,164.3 | 0.0 |
| ... | | | | | | | | |
| 2009 | FCL | 17-Apr-2009 | 16-Apr-2010 | 31,528.0 | 0.0 | 0.0 | 0.0 | 0.0 |

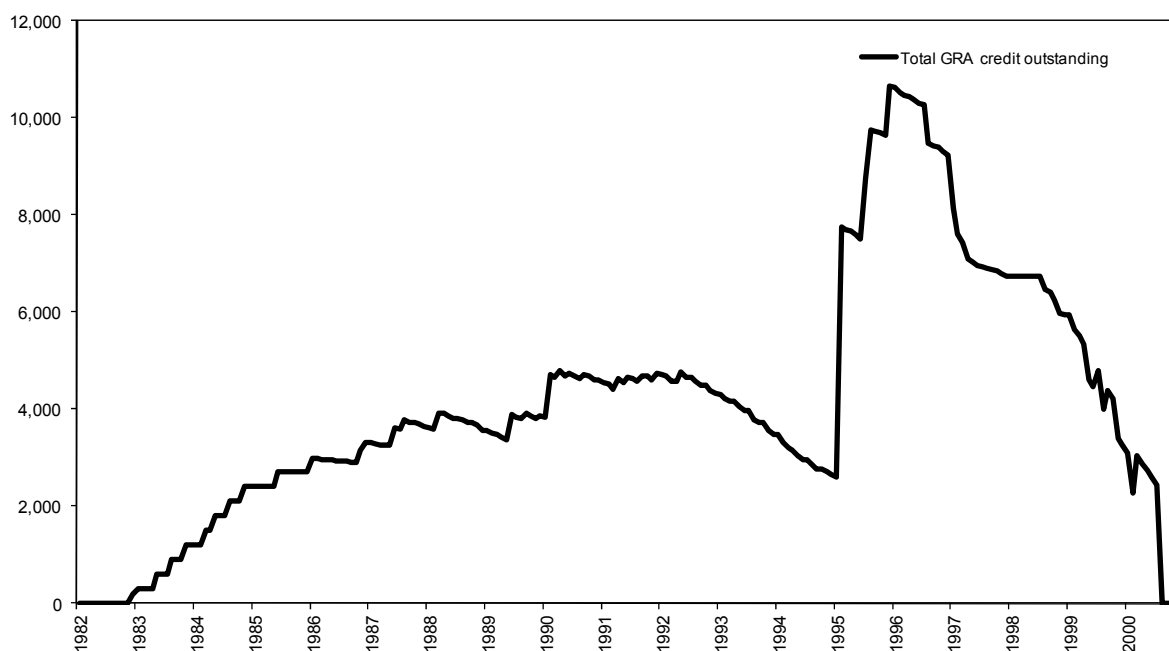
Source: Finance Department.

1/ As of end-December.

2/ Includes a first credit tranche purchase of SDR 291.4 million.

3/ Includes a purchase of SDR 453.5 million under the Compensatory Financing Facility.

Figure I.1. Mexico: IMF Credit Outstanding, 1982–2000
(In millions of SDRs)



Source: Finance Department.



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FOR IMMEDIATE RELEASE
March 25, 2010

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Renews US\$48 Billion Flexible Credit Line Arrangement with Mexico

The Executive Board of the International Monetary Fund (IMF) today approved a successor one-year arrangement for Mexico under the Flexible Credit Line (FCL) in an amount equivalent to SDR 31.528 billion (about US\$48 billion). The Mexican authorities stated they intend to treat the arrangement as precautionary and do not intend to draw on the line.

The FCL was established on March 24, 2009 as part of a major reform of the Fund's lending framework (see [Press Release No. 09/85](#)). The FCL is designed for crisis prevention purposes as it provides the flexibility to draw on the credit line at any time. Disbursements are not phased nor conditioned on compliance with policy targets as in traditional IMF-supported programs. This flexible access is justified by the very strong track records of countries that qualify for the FCL, which gives confidence that their economic policies will remain strong.

Following the Executive Board discussion of Mexico, Mr. John Lipsky, First Deputy Managing Director and Acting Chairman of the Board, made the following statement:

“Mexico has a sustained record of sound economic policies, and has very strong economic fundamentals and frameworks. Public and private debt levels were reduced and balance sheets strengthened in the years before the global crisis. Well implemented rules-based policy mechanisms, including the balanced budget fiscal rule and inflation targeting framework and flexible exchange rate regime, have anchored stability.

This strong policy framework has helped preserve stability during the crisis, and—for the first time in many decades—allowed the authorities to deliver a sizable countercyclical fiscal and monetary policy response. Adroit steps have been taken in various financial market segments to maintain orderly conditions. The authorities have continued to demonstrate their commitment and ability to reform in challenging times, including through the passage of important revenue measures in the 2010 budget that will strengthen the medium-term fiscal

outlook. Swift action to secure contingent credit lines during the crisis—from the U.S. Federal Reserve and the International Monetary Fund—also helped maintain external confidence.

On the back of these strong policy measures and improving global economic conditions, growth has resumed since mid-2009, asset prices have recovered from troughs seen at the height of the crisis, and domestic financial stability has been maintained. Looking forward, policies will continue to be underpinned by the rules-based macroeconomic framework, and the authorities intend to continue to react as needed to any future shocks that may arise.

Nonetheless, sizeable downside risks still confront the global economy. It is against this background that, at the authorities' request, the Executive Board today approved a one-year arrangement under the IMF's FCL, which the authorities intend to treat as precautionary. This successor FCL arrangement will continue to play an important role in supporting the authorities' overall macroeconomic strategy and in bolstering confidence until external conditions improve, complementing financing from other multilaterals.

Mexico's very strong policy frameworks and economic fundamentals, together with the additional insurance provided by the successor arrangement under the FCL, put Mexico in a very strong position to deal with other potential risks that could arise in the period ahead as the global economy continues to gradually recover from the crisis."

To read the staff report and other documents related to the approval of Mexico's Flexible Credit Line, please see: <http://www.imf.org/external/pubs/ft/scr/2010/cr1081.pdf>